

Supreme Court of the United States

OCTOBER TERM, 1965

No. 645

UNITED STATES, PETITIONER

vs.

THE EQUITABLE LIFE ASSURANCE SOCIETY
OF THE UNITED STATES

ON WRIT OF CERTIORARI TO THE SUPREME COURT
OF THE STATE OF NEW JERSEY

I N D E X

Original Print

Record from the Superior Court of New Jersey, Appellate Division, consisting of Appendix to Brief of Plaintiff-Appellant filed in that Court incorporating portions of record from Superior Court, Chancery Division of Bergen County

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SUPERIOR COURT OF NEW JERSEY
APPELLATE DIVISION.

* * * *

Civil Action.

**THE EQUITABLE LIFE ASSURANCE SOCIETY OF THE UNITED
STATES, a corporation of the State of New York,
PLAINTIFF-APPELLANT**

vs.

**ALBERT BAGIN (a/k/a Alben Bagin), et al.,
DEFENDANTS-RESPONDENTS**

**On Appeal from Superior Court Chancery Division
Bergen County**

Sat Below:

Pashman, J.S.C.

APPENDIX FOR PLAINTIFF-APPELLANT

* * * *

[fol. 1]

IN THE SUPERIOR COURT OF BERGEN COUNTY,
NEW JERSEY

COMPLAINT—Filed June 4, 1963

* * * *

FIRST COUNT

1. On December 13, 1960, Albert Bagin and Erika Bagin, his wife, being indebted to plaintiff in the sum of \$30,000, executed to it a bond of that date to secure that sum with interest at the rate of 6% per annum, payable in 336 successive monthly instalments due and payable on the first day of each month commencing February 1, 1961.

2. To secure the payment of the bond, the said Albert Bagin and Erika Bagin, his wife, executed to plaintiff a mortgage of even date with the bond, and thereby conveyed to it in fee the land hereinafter described, on the express condition that such conveyance should be void if payment should be made according to the terms of the bond and mortgage. The said mortgage was duly recorded in the Clerk's office of Bergen County at 11:51 a.m. on December 19, 1960, in Book 3651 of Mortgages for said county, at page 285.

* * * *

4. The mortgage contained an agreement that if any instalment of principal and interest should remain unpaid for 30 days after the same should fall due, the whole of the principal sum then unpaid, together with all unpaid interest, should, at the opinion of the mortgagee, become immediately due.

* * * *

6. On March 1, 1963, defendants Albert Bagin and Erika Bagin, his wife, failed to pay the monthly instalment of principal and interest due on said date and the [fol. 2] said monthly instalment has remained unpaid for more than 30 days. Said defendants have failed and neglected to pay any monthly instalments, or any portion

thereof, since February 1, 1963, to the date hereof. Plaintiff has, therefore, elected that the whole principal sum with all unpaid interest and all additions thereto, as provided by the mortgage and alleged in this complaint, is now due.

* * * *

9. On December 13, 1960, defendants Albert Bagin and Erika Bagin, his wife, gave a mortgage to Wulster Built Homes, Inc., a New Jersey corporation, which mortgage was recorded at 1:58 p.m. on December 19, 1960, in Book 3651 of Mortgages for Bergen County at page 399. This mortgage covers the premises in the Borough of Upper Saddle River, Bergen County, New Jersey, described in paragraph 3 hereof, and was allegedly given to secure an indebtedness in the amount of \$6,000.00. By an instrument dated January 17, 1961, and recorded January 17, 1961, in Book 523 of Assignments of Mortgages at page 298, Wulster Built Homes, Inc., a New Jersey corporation, assigned said mortgage to defendant William Hawkey.

* * * *

11. Defendant Albert Bagin is also known as Alben Bagin.

12. On March 21, 1962, defendant United States of America filed a notice of Federal Lien, dated March 19, 1962, in the office of the Clerk of Bergen County against, *inter alia*, Alben Bagin for withholding taxes of \$7,748.91. The notice was recorded in Book 27 of Federal Liens at page 572.

13. Any interest, lien, or encumbrance which any of the foregoing named defendants has or claims to have in or upon the mortgaged premises, or any part thereof, is subject to the lien of plaintiff's mortgage.

* * * *

[fol. 3]

IN THE SUPERIOR COURT OF BERGEN COUNTY

ANSWER. Filed by Defendant William Hawkey
Served June 21, 1963

* * * *

(Admits allegations of paragraphs 3, 9, and 13 of the First Count of the Complaint and all allegations of the Second Count. Defendant has no knowledge or information sufficient to form a belief as to the other allegations of the Complaint.)

WHEREFORE, this defendant joins in the demand of the plaintiff for judgment and also demands that such judgment shall fix the amount due to him on his mortgage, and that he be paid the amount so fixed with interest and costs, and that the lands be sold to satisfy such amount as well as the amount due to the plaintiff.

* * * *

IN THE SUPERIOR COURT OF BERGEN COUNTY

ANSWER. Filed by Defendant United States of America.

Served, with a Stipulation Extending Time to Answer,
August 26, 1963

* * * *

This defendant, which has been made a defendant as a subsequent encumbrancer in the above cause, does not dispute the priority of the plaintiff's mortgage as stated in the complaint filed in this cause, except that the defendant disputes the priority of counsel fees and of any advances whatsoever made after the assessment dates of the lien of the United States, and says there is due to it on its Federal Tax Lien set forth in paragraph No. 12 of said complaint the sum of \$7,708.91, together with penalties and interest.

[fol. 4] The defendant reserves the right to redeem within one year of the date of sale, as provided by 28

U.S.C. Section 2410, and requests that its encumbrance be reported upon.

* * * *

MOTION.

Argued December 13, 1963.

IN THE SUPERIOR COURT OF BERGEN COUNTY

OPINION.—Decided January 9, 1964, Amended
March 9, 1964.

This is a motion for summary judgment and to settle the form of judgment in a suit to foreclose a mortgage. The mortgage covering premises in the Borough of Upper Saddle River was executed by defendants Albert and Erika Bagin to plaintiff on December 13, 1960 and recorded in the Bergen County Clerk's office on December 19, 1960 at 11:51 A.M. These defendants also executed a mortgage to Wulster Built Homes, Inc., which was recorded at 1:58 P.M. on December 19, 1960. By an assignment dated and recorded January 17, 1961 Wulster Built Homes, Inc. assigned its mortgage to defendant William Hawkey.

On March 20, 1961 a third mortgage covering the Upper Saddle River premises was given by defendants Bagin to defendants Merle B. Kenwood and Rose B. Rosenthal, t/a Charles & Co. This mortgage was recorded on May 18, 1961.

On March 21, 1962 the defendant United States of America filed a notice of federal tax lien, dated March 19, 1962, in the office of the Clerk of Bergen County, against, *inter alia*, Alben Bagin for withholding taxes due in the sum of \$7,748.91.

Defaults have been entered against the defendants Albert and Erika Bagin and Merle B. Kenwood and Rose B. Rosenthal, t/a Charles & Co.

[fol. 5] Plaintiff contends that it is entitled to possession, foreclosure of the mortgage, and a sheriff's sale of the property due to the default of defendants Bagin under the terms of the mortgage. Plaintiff alleges that

\$30,052.14 is due on the mortgage plus interest from September 6, 1963 and costs including a counsel fee under R. R. 4:55-7(c). Defendant Hawkey does not dispute plaintiff's priority and asks that the amount due to him be reported on. Plaintiff contends that the sum of \$5,104 plus interest from September 1, 1963 is due to defendant Hawkey.

The United States of America does not dispute the priority of either of these two mortgages as to principal and interest but contends that the Federal Government's tax lien has priority over the allowance to the mortgagees of counsel fees and any advancements for real estate taxes and/or insurance premiums made after the assessment of the tax lien. The basis of these contentions is two recent decisions by the United States Supreme Court in *United States v. Buffalo Savings Bank*, 371 U.S. 228, 83 S. Ct. 314 (1963) and *United States v. Pioneer American Insurance Company*, 374 U.S. 84, 83 S. Ct. 1651 (1963).

The pleadings and affidavits on file show palpably that there is no genuine issue as to any material fact. There is no need for a plenary trial and the proofs clearly indicate that plaintiff is entitled to a summary judgment of foreclosure as a matter of law. See R. R. 4:58-3; *United Advertising Corp. v. Metuchen*, 35 N. J. 193 (1961); *Bouley v. Borough of Bradley Beach*, 42 N. J. Super. 159, 168 (App. Div. 1956); *Devlin v. Surgent*, 18 N. J. 148 (1955).

The lien of the United States for unpaid taxes arose under 26 U.S.C.A. § 6321 and is a lien "upon all property and rights to property, whether real or personal," belonging to the taxpayer Albert Bagin. By virtue of 26 U.S.C.A. § 6322, a federal tax lien arises at the time of assessment. The mortgages were prior in time to the tax [fol. 6] lien and generally speaking they have priority as to principal and interest due. See 26 U.S.C.A. §§ 6322, 6323; N.J.S.A. 46:16-13.

The dispute concerning the priority of counsel fees and any advancements for taxes and insurance payments is solely a question of law and may be decided on a motion for summary judgment.

Counsel for plaintiff, in support of its position, has presented the court with the transcript of a recent, unreported decision of another Chancery vicinage in this State which held that counsel fees allowed by our court rules and advances for local property taxes in an action to foreclose a mortgage have priority over a subsequently filed federal tax lien.

The Federal Government contends, although diligent research on the part of counsel and this court has failed to find a reported decision on point, that the courts of this State have been deciding these questions contrary to the dictates of the United States Supreme Court.

In *United States v. Buffalo Savings Bank*, *supra*, the court, in a mortgage foreclosure action where federal tax liens arose after the mortgage, in reliance upon *United States v. City of New Britain*, 347 U.S. 81, 74 S. Ct. 367, 98 L. Ed. 520 (1954) held:

"* * * that federal tax liens have priority over subsequently accruing liens for local real estate taxes, even though the burden of the local taxes in the event of a shortage would fall upon the mortgagee whose claim under state law is subordinate to local tax liens." 83 S. Ct. at p. 315.

The court has examined the case of *United States v. Pioneer American Insurance Co.*, *supra*, where a provision for "a reasonable attorney's fee" was incorporated into [fol. 7] the mortgage which was being foreclosed. The court, once again relying on *United States v. City of New Britain*, *supra* and other cases which discuss the choate lien test held that the claim for attorney's fees remained inchoate until finally fixed in amount in the mortgage foreclosure decree. Based upon this reasoning, the court held the claim for attorney's fees to be subordinate to federal tax liens. The same reasoning would clearly be applicable to our R. R. 4:55-7(c) which provides for counsel fees in a mortgage foreclosure action.

Since it is well settled that the priority of federal tax liens against competing claimants and lienors is to be determined by federal law, *United States v. City of New Britain*, *supra*; *United States v. Acree*, 348 U.S. 211, 75

S. Ct. 239, 99 L. Ed. 264 (1955), this court holds that it is bound by the decision in *United States v. Pioneer American Insurance Co.*, *supra* and not at all bound by the unreported Chancery decision cited by plaintiff.

The plaintiff contends that there were no advances for taxes or insurance payments. Thus it is not necessary to decide the question of priority concerning these types of advances although the *Buffalo Savings Bank* case, *supra*, is clear on the question of property tax liens arising subsequent to the filing of a federal tax lien.

Counsel have agreed to settle between them any problem arising out of the fact that the property was held as a tenancy by the entirety and the federal tax lien was against the husband alone. Thus, the issues which might arise because of these facts are not before the court.

Based upon the foregoing plaintiff is entitled to partial summary judgment as follows:

- (1) The sum of \$30,052.14 due on its mortgage plus costs and lawful interest from September 6, 1963.
- [fol. 8] (2) The lands are to be sold according to law to satisfy the amount due to plaintiff.
- (3) Plaintiff is entitled to possession of the lands from defendants Bagin or anyone holding same under them.
- (4) Defendant William Hawkey is entitled to \$5,104 due on his mortgage plus lawful interest from September 6, 1963.
- (5) Any counsel fee awarded plaintiff pursuant to R. R. 4:55-7(c) shall be paid in a manner not inconsistent with this opinion at a surplus money proceeding, if any.
- (6) All defendants are barred and foreclosed of all equity of redemption in and to said lands, except that the United States of America retains its right to redeem pursuant to 28 U.S.C.A. § 2410.

The order of priority of payment of liens is as follows:

1. First mortgage plus interest from September 6, 1963 and costs.

2. Second mortgage plus interest from September 6, 1963.

3. Lien of United States Government.

4. Counsel fee due under the Rules of court and advances made by virtue of first mortgage.

The third mortgagee filed no answer. A default has been entered against it. Said mortgagee will be limited to its priority in surplus money proceedings.

Counsel may present a form of judgment pursuant to R. R. 4:55-1.

[fol. 9]

IN THE SUPERIOR COURT OF BERGEN COUNTY

FINAL JUDGMENT. Entered April 6, 1964.

* * * *

This matter having been presented to the court on plaintiff's motion for summary judgment and to settle the form of judgment, Frank W. Hoak appearing for Donald B. Jones, attorney for plaintiff, Martin Tuman appearing for David M. Satz, Jr., United States Attorney, and the court having read and considered the briefs submitted and having heard and considered the arguments of counsel, and having rendered a written opinion dated January 9, 1964;

And it appearing that summons and complaint has been duly issued and returned served upon all the defendants, and default having been taken against all defendants except William Hawkey, who has filed an answer which does not dispute the priority of the plaintiff's mortgage, but requests that his lien be reported upon, and except the United States of America, which has filed an answer that does not dispute the priority of the plaintiff's mortgage but disputes the priority of counsel fees and of any advances whatsoever made after the assessment dates of the lien of the United States; and the plaintiff's bond and mortgage, and the notes mortgage, and assignment of mortgage held by the defendant William Hawkey, having been produced and marked as exhibits by the court.

And it appearing from the affidavits filed herein that there is due to the plaintiff for the principal and interest on its mortgage described in the complaint the sum of \$30,052.14; and that there is due to the defendant William Hawkey for the principal and interest on his mortgage described in the complaint the sum of \$5,104.00; no proof by way of an affidavit being submitted on behalf of the defendant United States of America.

And the court having found that the pleadings and affidavits on file show palpably that there is no genuine [fol. 10] issue as to any material fact, that there is no need for a plenary trial, and that the proofs clearly indicate that plaintiff is entitled to a summary judgment of foreclosure as a matter of law.

And the court having determined that it is not necessary to decide the question of priority concerning advances for taxes or insurance payments because plaintiff contends that there were no advances for taxes or insurance payments;

And the court having determined that the issues which might arise because the property was held as a tenancy by the entirety and the federal tax lien was against the husband alone are not before the court, because counsel have agreed to settle between them any problem arising out of these facts.

And the court having determined that plaintiff is entitled to partial summary judgment as follows:

(1) The sum of \$30,052.14 due on its mortgage plus costs and lawful interest from September 6, 1963.

(2) The lands are to be sold according to law to satisfy the amount due to plaintiff.

(3) Plaintiff is entitled to possession of the lands from defendants Bagin or anyone holding same under them.

(4) Defendant William Hawkey is entitled to \$5,104 due on his mortgage plus lawful interest from September 1, 1963, and costs.

(5) Any counsel fee awarded plaintiff pursuant to R. R. 4:55-7(c) shall be paid in a manner not inconsistent with the court's opinion, dated January 9, 1964, at a surplus money proceeding, if any.

(6) All defendants are barred and foreclosed of all equity of redemption in and to said lands, except that the [fol. 11] United States of America retains its right to redeem pursuant to 28 U.S.C.A. § 2410.

And the court having determined that the order of priority of payment of liens is as follows:

1. First mortgage plus interest from September 6, 1963, and costs.
2. Second mortgage plus interest from September 1, 1963, and costs.
3. Lien of United States Government.
4. Counsel fee due under the Rules of court and advances made by virtue of first mortgage.

The third mortgagee, Merle B. Kenwood and Rose B. Rosenthal, t/a Charles & Co., having filed no answer and having had default entered against it will be limited to its priority to be established at a surplus money proceeding, if any.

It is, on this 6th day of April, 1964, ORDERED and ADJUDGED, first, that the plaintiff is entitled to have the sum of \$30,052.14, together with lawful interest thereon to be computed from September 6, 1963, together with costs of this suit to be taxed, including a counsel fee of \$425.52 which is hereby allowed to plaintiff pursuant to R. R. 4:55-7(c), raised and paid out of the mortgaged premises described in the complaint; second, that the defendant William Hawkey is entitled to have the sum of \$5,104.00, together with lawful interest thereon to be computed from September 1, 1963, together with costs of this suit to be taxed, raised and paid out of the mortgaged premises described in the complaint.

And it is further ORDERED and ADJUDGED that so much of the said mortgaged premises as will be sufficient to raise and satisfy the said mortgage, interest, and costs of the plaintiff, and the said mortgage, interest, and costs of [fol. 12] the defendant William Hawkey, be sold, and that an execution do issue for that purpose out of this court, directed to the Sheriff of the County of Bergen, commanding him to make sale, according to law, of so much of the mortgaged premises as will be sufficient to satisfy

first, the said mortgage, interest, and costs of the plaintiff, and second, the said mortgage, interest, and costs of the defendant William Hawkey; and that he first pay out of the proceeds of the sale to the plaintiff or its attorney the sum of \$30,052.14, together with interest as aforesaid and costs exclusive of the counsel fee, and second that he pay out of the proceeds of the sale to the defendant William Hawkey or his attorney the sum of 5,104.00, together with interest as aforesaid and costs; and that in case there is a surplus, the same shall be brought into this court and deposited with the clerk, subject to the order of this court; and that said sheriff make his report to this court of the sale as required by the rules of this court;

And it is further ORDERED and ADJUDGED that the plaintiff duly recover against the defendants Albert Bagin (a/k/a Alben Bagin) and Erika Bagin, his wife, or any one holding under them, possession of the premises mentioned and described in the complaint with the appurtenances and that an execution issue thereon.

And it is further ORDERED and ADJUDGED that all of the defendants to this action, and each of them, stand absolutely debarred and foreclosed of and from all equity of redemption of, in, and to so much of the mortgaged premises as shall be sold as aforesaid under this judgment, except United States of America reserves the [fol. 13] right to redeem within one year of the date of the sale as provided by 28 U.S.C. Section 2410.

MORRIS PASHMAN, J.S.C.
J.S.C.

We hereby consent to the form of this Final Judgment.

DAVID M. SATZ
United States Attorney
DAVID M. SATZ JR.

by: MARTIN G. HOLLERAN
Assistant U.S. Attorney

DAVID A. GELBER
Attorney for Defendant
WILLIAM HAWKEY

[fol. 14]

IN THE SUPERIOR COURT OF BERGEN COUNTY

NOTICE OF APPEAL.—Filed April 9, 1964

Notice is hereby given that plaintiff, The Equitable Life Assurance Society of the United States, a corporation of the State of New York, appeals to the Superior Court, Appellant Division, from that part of the Final Judgment entered in the above entitled action by the Superior Court, Chancery Division, on April 6, 1964, that provides for the priority of liens, other than the provision for the lien of the first mortgage plus interest from September 6, 1963, and costs.

[fol. 15]

IN THE SUPREME COURT OF NEW JERSEY

No. A-47, September Term, 1964

THE EQUITABLE LIFE ASSURANCE SOCIETY OF THE UNITED STATES, a corporation of the State of New York,
PLAINTIFF-APPELLANT

vs.

ALBERT BAGIN (a/k/a Alben Bagin), et al.,
DEFENDANTS-RESPONDENTS

Mr. Frank W. Hoak argued the cause for the plaintiff-appellant (*Mr. Donald B. Jones*, attorney).

Mr. Edward J. Turnbach, Assistant United States Attorney, argued the cause for the defendant-respondent United States of America (*Mr. David M. Satz, Jr.*, United States Attorney, attorney; *Mr. Martin G. Holleran*, Assistant United States Attorney, on the brief).

OPINION PER CURIAM:—July 6, 1965

The plaintiff, The Equitable Life Assurance Society of the United States, held a \$30,000 first mortgage and an

accompanying bond which were executed, on December 19, 1960, by the defendants Albert Bagin and Erika Bagin, his wife. Upon default, the plaintiff filed a foreclosure complaint setting forth the execution of the bond and mortgage, the execution by the Bagins of a second mortgage dated December 19, 1960 and held by William Hawkey, and the filing by the United States, on March 21, 1962, of notice of a \$7,748.91 federal lien for withholding taxes. See 26 U.S.C.A. §§ 6321-6323. The defendant Hawkey filed an answer joining in the plaintiff's demand [fol. 16] for judgment and demanding that the amount due on his mortgage be fixed and that the lands be sold to satisfy that amount as well as the amount due to the plaintiff. The defendant United States filed an answer in which it requested that its encumbrance be reported on.

On motion, the Chancery Division determined that the plaintiff was entitled to the sum of \$30,052.14 plus interest, and also to taxed costs which amounted to \$630.30, inclusive of the fee of \$425.52 provided for in R.R. 4:55-7(c); the sum due the defendant Hawkey was determined to be \$5,104 plus interest, and taxed costs which amounted to \$25. The United States expressly conceded the propriety of the mortgages including principal, interest and taxed costs, exclusive, however, of the \$425.52 item. With respect to that item it contended that the plaintiff was not entitled to priority under the principles expressed by the Supreme Court in *United States v. Pioneer American Ins. Co.*, 374 U.S. 84, 10 L.Ed.2d 770 (1963) and *United States v. Buffalo Savings Bank*, 371 U.S. 228, 9 L.Ed. 2d 283 (1963). The Chancery Division agreed with its contention, and entered an order of priority of payment of liens which deferred the \$425.52 item until after payment of both mortgages and the lien of the United States. Without awaiting the sale of the property, the plaintiff appealed to the Appellate Division and before argument there we certified.

After hearing oral argument we directed that the sale of the property be proceeded with. This has been done and the net sum (after payment of the fees and commissions due to the sheriff and clerk) now in hand for

distribution is \$39,193.31. The plaintiff contends that its priority includes the \$425.52 item and that consequently the order of distribution should be as follows: to the [fol. 17] first mortgagee, \$30,052.14 plus interest of \$2,830.58 plus taxed costs of \$630.30—total \$33,513.02; to the second mortgagee, \$5,104 plus interest of \$485.12 plus taxed costs of \$25—total \$5,614.12; to the United States the balance of \$66.17. On the other hand, the United States contends that the first mortgagee's priority as against it does not include the \$425.52 item and that distribution should be made by providing "for a priority adjustment fund consisting of the principal and interest, plus costs, of the two prior mortgages to be distributed in accordance with state law, but the surplus, if any, representing the Taxpayer's interest in the property at the time the federal tax lien arose, should be applied to the federal tax lien in full." Under this approach the fund would consist of \$33,087.50 for the first mortgagee, \$5,614.12 for the second mortgagee, and a surplus of \$491.69 for the United States, with the State remaining at liberty, however, to decide under its own laws that the \$425.52 be paid to the plaintiff by reducing the second mortgagee's judgment in that amount.

Taxed costs are traditional and incidental allowances which are of some help in defraying portions of the heavy expenses of litigation incurred by the prevailing parties. They are of long usage and are generally provided for by statutes and court rules. In the federal courts they include (28 U.S.C.A. § 1920) such items as fees of the clerk, marshal, court reporter and witnesses, printing costs, and "attorney's and proctor's docket fees." This last item is specifically governed by 28 U.S.C.A. § 1923 and, while the amounts listed there are meager, they occasionally add up to more significant sums. See, e.g., *Missouri v. Illinois*, 202 U.S. 598, 50 L.Ed. 1160 (1906) [fol. 18] where the taxed costs included \$720 for "solicitors' fees, viz., \$20 for attendance at final hearing and \$2.50 for each deposition taken and admitted in evidence." Under various federal statutory provisions further allowances for attorneys' fees may be made and included in the taxed costs. See *Peck, Taxation of Costs*

in *United States District Courts*, 42 *Neb.L.Rev.* 788, 799 (1963); 6 *Moore's Federal Practice* par. 54.71 (2d ed. 1953).

In the state courts, taxed costs are generally dealt with in similar fashion. See 20 *Am.Jur. 2d, Costs*, § 5 *et seq.* (1965); 4 *Utah L.Rev.* 501 (1955); 5 *N.H.Bar J.* 114 (1963); 42 *Mich. State Bar J.* 12 (Nov. 1963). In our own State there are governing statutes and court rules (*N.J.S.A.* 22A:2-1 *et seq.*; *R.R.* 4:55-6) some of which deal specifically with mortgage foreclosure proceedings. See *U.S. Pipe, etc. v. United Steelworkers of America*, 37 *N.J.* 343, 355 (1962). Thus *N.J.S.A.* 22A:2-10 provides for allowance in the taxed costs of \$50 for the attorney's "drawing of papers" in foreclosure actions, *R.R.* 4:55-9 provides that in such actions legal fees and charges incurred in procuring title searches may be included in the taxed costs, and *R.R.* 4:55-7(c) provides that in such actions, allowance for legal services in the taxed costs shall be calculated at 3% on the first \$5,000 adjudged to be due the plaintiff, 1½% on the excess over \$5,000 and up to \$10,000, and 1% on the excess over \$10,000. While this is designed towards further defrayal of some of the plaintiff's actual foreclosure costs, it is still not aimed at full compensation for the legal expenses incurred by the plaintiff; the percentages are fixed at low levels (2A *Waltzinger, New Jersey Practice* 28 (1954)), are not related to the actual extent of the legal services performed by the plaintiff's attorney, and are thus applicable even where the foreclosure is contested or complex. While *R.R.* 4:55-7(c) is part of our current court rules, its counterparts may be found in early statutes and rules of the former Court of Chancery. See *L. 1902, c. 158*, § 91; *Kocher's, Chancery Practice* 74 (1913). The allowance under the rules in the taxed costs is, of course, part and parcel of the plaintiff's judgment in foreclosure. See *R.R.* 4:55-8.

When Congress directed that the government's lien under section 6321 "shall not be valid as against any mortgagee" it did not specifically spell out the elements of the mortgagee's claim entitled to priority. See 26 *U.S.C.A.* § 6323. But it seems entirely clear that at least

principal, interest and costs were within the congressional contemplation. That much is not disputed by the government which set forth in its brief that here "the first and second mortgages were recorded before the federal tax lien was recorded and hence the principal and interest, plus costs of these mortgages are superior to the federal tax lien." And in a report submitted to this Court by the government following the sale of the foreclosed property it set forth the first mortgagee's priority as including principal, interest and taxed costs amounting to \$204.78. This latter sum consisted of filing fees, sheriff's fees and mileage, and \$50 under *N.J.S.A. 22A:2-10* for drawing pleadings plus \$100.78 search fees under *R.R. 4:55-9*. While the government excluded the sum of \$425.52 due the first mortgagee under *R.R. 4:55-7(c)*, we fail to find any sensible basis for differentiating that item from the other items acknowledged by the government. Thus the \$50 item represents services by the plaintiff's attorney as might the \$100.78 item. Without impairing their true character as traditional and incidental costs, the State could readily and conveniently have provided for larger sums, *e.g.*, by statutory or rule provision allowing individual amounts for each of the plead-[fol. 20] ings filed or each of the steps taken. In their aggregate these could well have exceeded those provided by the modest percentages fixed in *R.R. 4:55-7(c)* and, for present purposes, it would appear wholly immaterial which of these courses the State has chosen in dealing with its allowance of taxed costs.

The government continues its reliance on *Buffalo Savings, supra*, and *Pioneer, supra*, but these cases involved different situations. In *Buffalo Savings* the mortgage was executed in 1946, the government's lien was filed in 1953, and thereafter in 1957 and 1958 local liens for unpaid real estate taxes attached to the property. On foreclosure, the trial court directed that the local real estate taxes be paid as part of the expenses of sale prior to the satisfaction of the government's lien. This was reversed by the Supreme Court in a *per curiam* which pointed out that "the state may not avoid the priority rules of the federal tax lien by the formalistic device of

characterizing subsequently accruing liens as expenses of sale." 374 U.S. at 229, 9 L.Ed. 2d at 284. Here we are not dealing with any formalistic device or any circumvention of federal priority but with a traditional and incidental allowance by way of taxed costs for services which were truly part of the plaintiff's actual legal costs and expenses in foreclosing its mortgage. Indeed it may be assumed that its actual foreclosure expenses here exceeded its taxed costs. Its efforts in pursuing the foreclosure through sale have benefited not only the mortgagees but the government as well. In a fair sense, it has produced a fund from which the government will receive a return without any expenditure on its own part. It would therefore appear that not only are the significant legal considerations unfavorable to the government's position here but so also are the equitable ones. See *Washington Const. Co. v. United States of America*, 75 N.J. Super. 536 (Ch.Div. 1962); *Smith v. Smith*, 78 N.J. Super. 28 (Ch.Div. 1963); but cf. *United States v. Pioneer American Ins. Co.*, *supra*, 374 U.S. at 92, 10 L.Ed.2d at 777 u. 13; *Camptown Savings & Loan Assn. v. United States, etc.*, 85 N.J. Super. 18, 20 (App.Div. 1964).

In *Pioneer* the holder of a note and mortgage instituted foreclosure proceedings in a state court. The note was in the face amount of \$20,000 and contained a provision that in the event of court proceedings the mortgagor would pay "a reasonable attorney's fee." The foreclosure decree fixed the attorney's fee at \$1250 and "after satisfaction of court and foreclosure sale costs" the mortgagee was accorded first priority for principal, interest and the attorney's fee. The Supreme Court, in holding that the federal tax lien under section 6321 was entitled to priority over the attorney's fee, found the latter to be inchoate rather than choate. See *Kennedy, The Relative Priority of the Federal Government: The Pernicious Career of the Inchoate and General Lien*, 63 Yale L.J. 905, 911 (1954); *Note, Federal Priorities & Tax Liens*, 63 Colum.L.Rev. 1259, 1264 (1963). Among other matters, it pointed to the fact that the mortgagee was obligated to pay a "reasonable" fee, that this related

"to the service to be performed by the attorney," and that it could not be "finally fixed in amount" until the date of the decree. 374 U.S. at 87, 90-91, 10 L.Ed. 2d at 773-774, 776.

Pioneer did not deal with any item of taxed costs allowed by statute or court rule but with a contractual agreement for the payment of a fee. Cf. *Burgen Builders, Inc. v. Horizon Developers, Inc.*, 44 N.J. 435 (1965). [fol. 22] That contractual agreement provided, not for a fixed percentage as in *Security Mortg. Co. v. Powers*, 278 U.S. 149, 73 L.Ed. 236 (1928) (and as in our R.R. 4:55-7(c)), but for a reasonable fee which could not be ascertained until all of the legal work had been done and the final decree was about to be entered. While *Security Mortgage* dealt with a bankruptcy proceeding, it is to be noted that there Justice Brandeis remarked that "the lien was not inchoate" but "had already become perfect when the principal note and the loan deed serving it were given." 278 U.S. at 156, 73 L.Ed. at 241. See *United States v. Seaboard Citizens Nat. Bank*, 206 F.2d 62 (4th Cir. 1953).

The contours of the Supreme Court's doctrine of choateness remain to be fixed and undoubtedly further pronouncements by that Court will be handed down. See *United States v. Vermont*, 377 U.S. 351, 12 L.Ed. 2d 370 (1964); *Kennedy, From Spokane County to Vermont: The Campaign of the Federal Government Against the Inchoate Lien*, 50 Iowa L.Rev. 724 (1965); compare *Streeter v. Overfelt*, 202 F.Supp. 143, 146 (D. Mont. 1962), with *First National Bank of Lewistown v. Tilzey*, 238 F.Supp. 750 (D. Mont. 1965). Nothing thus far, including *Pioneer* which contains no discussion whatever on the subject of taxed costs, persuades us that the traditional and incidental allowances in foreclosure proceedings under R.R. 4:55-7(c) are not lawfully and justly entitled to the same priority as that afforded to the mortgage principal and interest.

Reversed and remanded for distribution in conformity with the views expressed in this *per curiam*.

[fol. 23]

IN THE SUPREME COURT OF NEW JERSEY

Appeal Docket No. 4566

Civil Action On Appeal

EQUITABLE LIFE ASSURANCE SOCIETY OF THE
UNITED STATES, PLAINTIFF-APPELLANT

vs.

ALBERT BAGIN, ET AL., DEFENDANTS-RESPONDENTS

MANDATE ON REVERSAL—July 6, 1965

This cause having been duly argued before this Court by Mr. Frank W. Hoak, counsel for the appellant and Mr. Edward J. Turnbach, counsel for the respondent, and the Court having considered the same,

It is hereupon ordered and adjudged that the judgment of the said Superior Court, Chancery Division is in all things reversed, set aside and for nothing holden, with costs; and it is further ordered that this mandate shall issue ten days hereafter, unless an application for rehearing shall have been granted or is pending, or unless otherwise ordered by this Court, and that the record and proceedings be remitted to the said Superior Court, Chancery Division to be there proceeded with in accordance with the rules and practice relating to that court, consistent with the opinion of this Court.

WITNESS the Honorable JOSEPH WEINTRAUB, Chief Justice, at Trenton on the sixth day of July, 1965.

JOHN H. GILDEA

Clerk of the Supreme Court

[File Endorsement Omitted]

[fol. 24]

IN THE SUPREME COURT OF NEW JERSEY

No. M-36 September Term 1965

[Title Omitted]

ORDER RE ISSUANCE OF MANDATE—Sept. 21, 1965

This matter having been duly considered by the Court, it is ORDERED that the mandate of this court issue with instructions that distribution be withheld of the sum of \$491.69 and that distribution be permitted of the conceded priority adjustment fund.

WITNESS the Honorable Joseph Weintraub, Chief Justice, at Trenton this twenty-first day of September 1965.

JOHN H. GILDEA
Clerk

[File Endorsement Omitted]

[fol. 25]

[Clerk's Certificate Omitted in Printing]

[fol. 26]

SUPREME COURT OF THE UNITED STATES

No. 645, October Term, 1965

UNITED STATES, PETITIONER

v.

THE EQUITABLE LIFE ASSURANCE SOCIETY OF THE
UNITED STATES

ORDER ALLOWING CERTIORARI—January 17, 1966

The petition herein for a writ of certiorari to the Supreme Court of the State of New Jersey is granted, and the case is placed on the summary calendar.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

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In the Supreme Court of the United States

OCTOBER TERM, 1965

No.

UNITED STATES OF AMERICA, PETITIONER

v.

THE EQUITABLE LIFE ASSURANCE SOCIETY OF THE
UNITED STATES

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME
COURT OF THE STATE OF NEW JERSEY

The Solicitor General, on behalf of the United States, petitions for a writ of certiorari to review the judgment of the Supreme Court of New Jersey in this case.

OPINION BELOW

The opinion (R. 4a-8a¹) of the Superior Court, Chancery Division, Bergen County, is not reported. The opinion of the Supreme Court of New Jersey (Appendix, *infra*, pp. 10-17) is not yet reported.

¹ "R." references are to the Appendix to Plaintiff-Appellant's brief below.

JURISDICTION

The judgment of the Supreme Court of New Jersey was entered on July 6, 1965 (Appendix, *infra*, pp. 17-18). The jurisdiction of this Court is invoked under 28 U.S.C. 1257(3).

QUESTION PRESENTED

A State law provides that, in mortgage foreclosure actions, an allowance for an attorney's fee, fixed as a percentage of the amounts adjudged by the foreclosure court to be due under the mortgage, shall be a part of the taxed costs of the action. The question presented is whether a federal tax lien is entitled to priority over the mortgagee's claim for such attorney's fee, where notice of the federal tax lien was recorded prior to default by the mortgagor.

RULE INVOLVED

Rules Governing the New Jersey Courts (1965 ed.):

4:55-7. *Counsel Fees*

No fee for legal services shall be allowed in the taxed costs or otherwise, except:

* * * *

(c) In an action for the foreclosure of a mortgage. The allowance shall be calculated as follows: on all sums adjudged to be paid the plaintiff in such an action, amounting to \$5,000 or less, at the rate of 3%, provided, however, that in any action a minimum fee of \$75 shall be allowed; upon the excess over \$5,000 and up to \$10,000 at the rate of 1½%; and upon the excess over \$10,000 at the rate of 1%.

* * * *

STATEMENT

This case began as a mortgage foreclosure action brought by respondent, the first mortgagee. The United States, a tax lien claimant, was named a party as provided in 28 U.S.C. 2410. The mortgage, covering real property owned by Albert Bagin and his wife, had been executed on December 13, 1960, and recorded a few days later. It secured the Bagins' indebtedness of \$30,000 to the respondent. On March 21, 1962, a federal tax lien for \$7,748.91 was filed against Mr. Bagin. A year later he and his wife defaulted on the mortgage and foreclosure proceedings were commenced.

In its answer filed in the foreclosure suit, the United States admitted that its lien was subordinate to the principal and interest on the mortgages² but claimed that its tax lien was superior to any claim for attorney's fees (R. 3a-4a). The Chancery Court agreed and, in its decree of foreclosure, granted the federal tax lien priority over respondent's attorney's fee, which the court fixed under the statute at \$425.52. Respondent appealed to the Superior Court of New Jersey, Appellate Division. While the case was pending there, the appeal was certified to the New Jersey Supreme Court on its own motion. That court directed that the property be sold forthwith. After the sale, it ruled that the mortgagee's attorney's fee was payable ahead of the federal tax lien out of the proceeds of the sale.

² A second mortgage had been recorded on December 19, 1960, and a third on May 18, 1961.

REASONS FOR GRANTING THE WRIT

1. The decision below conflicts with and misapplies the principles of this Court's decision in *United States v. Pioneer American Ins. Co.*, 374 U.S. 84, which established the standards governing the determination of priority as between the federal tax lien and the mortgagee's claim for an attorney's fee for prosecuting the action to foreclose the mortgage. In *Pioneer*, the mortgage agreement provided for payment to the mortgagee of a "reasonable attorney's fee" in the event of foreclosure (P. 90). After default and the institution of the foreclosure action, but before entry of the judicial decree determining the attorney's fee, the United States recorded its tax lien on the property. Applying the settled principle that the priority of the federal tax lien could be defeated only by a prior recorded choate lien, this Court held that the federal tax lien enjoyed priority. At the time that lien was recorded, the mortgagee's claim for a reasonable attorney's fee had been "undetermined and indefinite" (p. 90). It had not been "reduced to a liquidated amount" (p. 91). There was not even a "showing in this record that the mortgagee had become obligated to pay and had paid any sum of money for services performed prior to the filing of the federal tax lien" (*ibid.*). Thus, the mortgagee's claim had been not only "uncertain in amount" but "yet to be incurred and paid" (*ibid.*).

Despite some factual differences, the rationale of *Pioneer* requires that in the present case, too, the federal tax lien be accorded priority over the mort-

gatee's claim for an attorney's fee. Here, to be sure, the *method* of computing the fee due the mortgagee was not indefinite; under the statute, the fee is fixed at a specified percentage of "all sums adjudged to be paid" the mortgagee in the foreclosure action. But the *amount* of the fee was uncertain. It depended on the amount adjudged by the foreclosure court to be due the mortgagee, which would not be determined until the foreclosure action was completed.³

Moreover, in the present case the federal tax lien was recorded prior to default—at a time, that is, when the mortgagee's claim to an attorney's fee in the event of foreclosure was wholly contingent and uncertain. In *Pioneer*, in contrast, where the federal tax lien was not recorded until after the foreclosure action had been instituted, it was certain that the mortgagee would be entitled to an attorney's fee; only the amount remained to be determined. Thus, when the federal tax lien was recorded here, not only was the mortgagee's attorney's fee "undetermined and indefinite" and yet to be "reduced to a liquidated

³ The court below (Appendix, p. 17, *infra*) relied on *Security Mortgage Co. v. Powers*, 278 U.S. 149, for the proposition that the fixed percentage feature of the attorney's fee in this case made the *Pioneer* rule inapplicable—thereby disregarding the Court's observation in *Pioneer* (p. 90, n. 8) that the issue in *Security* was the status of an attorney's fee clause in bankruptcy proceedings "where the rigorous federal lien choateness test was not necessarily applicable." Nor does the fixed percentage feature make the attorney's fee here similar to interest on the principal amount of the mortgage, which concededly is entitled to priority over the federal tax lien. Interest is of the essence of the mortgage obligation. It is due so long as the mortgage remains in force, and it is not contingent on default or foreclosure.

amount", but, since the mortgage was not then in default, the mortgagee had not performed any of the services for which the fee was intended to compensate him; nor was it known whether he would ever be entitled to such fee.

2. The court below, in attempting to distinguish *Pioneer*, emphasized that in this case the mortgagee's right to an attorney's fee derived not from the mortgage agreement but from a State statute treating such fee as part of the taxable costs of the foreclosure action.⁴ This Court held in *United States v. Buffalo Savings Bank*, 371 U.S. 228, 229, that a State cannot, "by the formalistic device of characterizing subsequently occurring local liens as expenses of [the foreclosure] sale", confer priority over the federal tax lien on a lien for State real estate taxes. Here, the State has sought to confer priority on the claim for an attorney's fee by no less a "formalistic device" of treating the claim as a taxable cost of the foreclosure action. For, just as local taxes are different from expenses of sale, so attorney's fees are traditionally distinct from taxed costs, and the distinction rests on substantial and clear differences.

(1) Attorney's fees compensate for substantial professional services; costs, for the much less substantial, purely routine mechanical tasks in the prosecu-

⁴ In *Pioneer*, however, the provision obligating the mortgagor to pay an attorney's fee was judicially enforceable only because a State statute validated such agreements as contracts of indemnity. Prior to the enactment of the State statute, the State treated such agreements as unenforceable penalty provisions. See *Hollaway v. Pocahontas Federal Savings & Loan Ass'n*, 230 Ark. 310, 312, 323 S.W. 2d 204, 206.

tion of a lawsuit, such as filing pleadings and printing the record.⁵

(2) Attorney's fees are usually not taxed against the losing party in the suit; costs are.

(3) Attorney's fees are generally the most substantial element of the expenses of litigation; not so costs, which represent a much smaller, and usually nominal,⁶ amount. For this reason alone, the government has little incentive in the usual case to challenge their priority.

(4) The routine expenses reflected in taxed costs are necessary incidents to foreclosure, and hence benefit all lienholders; but as this Court noted in *Pioneer* (p. 92, n. 13), "[t]he attorney's services * * * were rendered for the benefit of the mortgagee to protect his interest in the property, and the United States, holding an adverse interest, received no such benefit from them that its interest is to be charged therefor."

(5) The government has not challenged the priority of taxed costs in mortgage foreclosure proceedings. Their priority was conceded in *Pioneer* itself. This Court implicitly accepted the distinction between

⁵ The New Jersey statute that includes in general costs an allowance of \$50 for drawing pleadings in a mortgage foreclosure case is not inconsistent. This "very old provision * * * was enacted at a time when there was little or no service of notices by mail, and contemplated the drawing of them in manuscript, copying them by hand, and the actual service of them on the respondents personally." *Steelman v. Moore Bros. Glass Co.*, 93 N.J. Eq. 533, 536.

⁶ Here, the attorney's fee was more than twice the other taxed costs, and the disproportion would probably have been much greater had a larger mortgage been involved.

taxed costs and attorney's fees in holding the latter, but not the former, subordinate to the federal tax lien.

In view of the settled and substantial differences between taxed costs and attorney's fees,⁷ it is plain that here, as in *Buffalo Savings*, the State statute has made a classification that is purely artificial and formal in assimilating attorney's fees to traditional taxed costs. If State classification of attorney's fees as part of the taxable costs of the foreclosure proceeding is accepted as determining the priority of such fees over the federal tax lien, the way to erosion of the *Pioneer* holding will be wide open.

3. Not only did the court below, in our view, misapply the basic rationale of *Pioneer* and ignore the teaching of *Buffalo Savings*, but its decision has wide practical implications. Quite apart from the danger that other States may seek to emulate New Jersey and pass similar statutes to the one in suit here, the laws of a number of States besides New Jersey already authorize the payment to the mortgagee of an attorney's fee out of the proceeds of the foreclosure sale.⁸ Moreover, in view of the suggestion of the

⁷ The New Jersey Supreme Court itself has recognized, in other contexts, that attorney's fees, "although if allowable are included in the taxed costs, are an entirely different matter." *United States Pipe v. United Steelworkers*, 37 N.J. 343, 356.

⁸ Cal. Code Civ. Proc. § 730; 2 Colo. Rev. Stat. (1963) § 13-16-6; Conn. Gen. Stat. Ann. § 49-7; 5 Del. Code Ann., Tit. 10, § 3912; 19 Fla. Stat. Ann. § 687.06; 44 Iowa Code Ann. § 625.22; New York Civ. Prac. Law and Rules §§ 8302-8303; 46 Okla. Stat. Ann. § 56; 4 Vt. Stat. Ann. § 4527; Rev. Code of Wash. Ann. § 4:84:020.

court below (Appendix, pp. 14-15, *infra*) that the result accomplished directly by the New Jersey statute here could be accomplished indirectly simply by increasing the amount of general costs taxable in a mortgage foreclosure proceeding, there is a clear need for this Court to define the line between attorney's fees that are subordinate to federal tax liens and traditional taxed costs.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that this petition for a writ of certiorari should be granted.

THURGOOD MARSHALL,
Solicitor General.

RICHARD M. ROBERTS,
Acting Assistant Attorney General.

JOSEPH KOVNER,
GEORGE F. LYNCH,
Attorneys.

OCTOBER 1965.

APPENDIX

SUPREME COURT OF NEW JERSEY

No. A-47, September Term, 1964

THE EQUITABLE LIFE ASSURANCE SOCIETY OF THE
UNITED STATES, a corporation of the State of New
York, PLAINTIFF-APPELLANT

vs.

ALBERT BAGIN (a/k/a Alben Bagin), et al.,
DEFENDANTS-RESPONDENTS

Argued December 15, 1964. Decided

Mr. Frank W. Hoak argued the cause for the plaintiff-appellant (*Mr. Donald B. Jones*, attorney).

Mr. Edward J. Turnbach, Assistant United States Attorney, argued the cause for the defendant-respondent United States of America (*Mr. David M. Satz, Jr.*, United States Attorney, attorney; *Mr. Martin G. Holleran*, Assistant United States Attorney, on the brief).

PER CURIAM:

The plaintiff, The Equitable Life Assurance Society of the United States, held a \$30,000 first mortgage and an accompanying bond which were executed, on December 19, 1960, by the defendants Albert Bagin and Erika Bagin, his wife. Upon default, the plaintiff filed a foreclosure complaint setting forth the execution of the bond and mortgage, the execution by the Bagins of a second mortgage dated December 19, 1960 and held by William Hawkey, and the filing by

the United States, on March 21, 1962, of notice of a \$7,748.91 federal lien for withholding taxes. See 26 U.S.C.A. §§ 6321-6323. The defendant Hawkey filed an answer joining in the plaintiff's demand for judgment and demanding that the amount due on his mortgage be fixed and that the lands be sold to satisfy that amount as well as the amount due to the plaintiff. The defendant United States filed an answer in which it requested that its encumbrance be reported on.

On motion, the Chancery Division determined that the plaintiff was entitled to the sum of \$30,052.14 plus interest, and also to taxed costs which amounted to \$630.30, inclusive of the fee of \$425.52 provided for in *R.R. 4:55-7(c)*; the sum due the defendant Hawkey was determined to be \$5,104 plus interest, and taxed costs which amounted to \$25. The United States expressly conceded the priority of the mortgages including principal, interest and taxed costs, exclusive, however, of the \$425.52 item. With respect to that item it contended that the plaintiff was not entitled to priority under the principles expressed by the Supreme Court in *United States v. Pioneer American Ins. Co.*, 374 U.S. 84, 10 L.Ed.2d 770 (1963) and *United States v. Buffalo Savings Bank*, 371 U.S. 228, 9 L.Ed.2d 283 (1963). The Chancery Division agreed with its contention, and entered an order of priority of payment of liens which deferred the \$425.52 item until after payment of both mortgages and the lien of the United States. Without awaiting the sale of the property, the plaintiff appealed to the Appellate Division and before argument there we certified.

After hearing oral argument we directed that the sale of the property be proceeded with. This has been done and the net sum (after payment of the fees and commissions due to the sheriff and clerk) now in hand

for distribution is \$39,193.31. The plaintiff contends that its priority includes the \$425.52 item and that consequently the order of distribution should be as follows:

to the first mortgagee, \$30,052.14 plus interest of \$2,830.58 plus taxed costs of \$630.30—total \$33,513.02; to the second mortgagee, \$5,104 plus interest of \$485.12 plus taxed costs of \$25—total \$5,614.12; to the United States the balance of \$66.17. On the other hand, the United States contends that the first mortgagee's priority as against it does not include the \$425.52 item and that distribution should be made by providing "for a priority adjustment fund consisting of the principal and interest, plus costs, of the two prior mortgages to be distributed in accordance with state law, but the surplus, if any, representing the Taxpayer's interest in the property at the time the federal tax lien arose, should be applied to the federal tax lien in full." Under this approach the fund would consist of \$33,087.50 for the first mortgagee, \$5,614.12 for the second mortgagee, and a surplus of \$491.69 for the United States, with the State remaining at liberty, however, to decide under its own laws that the \$425.52 be paid to the plaintiff by reducing the second mortgagee's judgment in that amount.

Taxed costs are traditional and incidental allowances which are of some help in defraying portions of the heavy expenses of litigation incurred by the prevailing parties. They are of long usage and are generally provided for by statutes and court rules. In the federal courts they include (28 *U.S.C.A.* § 1920) such items as fees of the clerk, marshal, court reporter and witnesses, printing costs, and "attorney's and proctor's docket fees." This last item is specifically governed by 28 *U.S.C.A.* § 1923 and, while the amounts listed there are meager, they occasionally add

up to more significant sums. See, e.g., *Missouri v. Illinois*, 202 U.S. 598, 50 L.Ed. 1160 (1906) where the taxed costs included \$720 for "solicitors' fees, viz, \$20 for attendance at final hearing and \$2.50 for each deposition taken and admitted in evidence." Under various federal statutory provisions further allowances for attorneys' fees may be made and included in the taxed costs. See *Peck, Taxation of Costs in United States District Courts*, 42 Neb.L.Rev. 788, 799 (1963); 6 *Moore's, Federal Practice* par. 54.71 (2d ed. 1953).

In the state courts, taxed costs are generally dealt with in similar fashion. See 20 *Am.Jur.2d, Costs*, § 5 et seq. (1965); 4 *Utah L.Rev.* 501 (1955); 5 *N.H. Bar J.* 114 (1963); 42 *Mich. State Bar J.* 12 (Nov. 1963). In our own State there are governing statutes and court rules (*N.J.S.A. 22A:2-1 et seq.*; *R.R. 4:55-6*) some of which deal specifically with mortgage foreclosure proceedings. See *U.S. Pipe, etc. v. United Steelworkers of America*, 37 N.J. 343, 355 (1962). Thus *N.J.S.A. 22-A:2-10* provides for allowance in the taxed costs of \$50 for the attorney's "drawing of papers" in foreclosure actions, *R.R. 4:55-9* provides that in such actions legal fees and charges incurred in procuring title searches may be included in the taxed costs, and *R.R. 4:55-7(c)* provides that in such actions, allowance for legal services in the taxed costs shall be calculated at 3% on the first \$5,000 adjudged to be due the plaintiff, 1½% on the excess over \$5,000 and up to \$10,000, and 1% on the excess over \$10,000. While this is designed towards further defrayal of some of the plaintiff's actual foreclosure costs, it is still not aimed at full compensation for the legal expenses incurred by the plaintiff; the percentages are fixed at low levels (2A *Waltzinger, New Jersey Practice* 28 (1954)), are not related to the actual extent

of the legal services performed by the plaintiff's attorney, and are thus applicable even where the foreclosure is contested or complex. While *R.R. 4:55-7* (c) is part of our current court rules, its counterparts may be found in early statutes and rules of the former Court of Chancery. See *L. 1902, c. 158, § 91; Kocher's, Chancery Practice* 74 (1913). The allowance under the rules in the taxed costs is, of course, part and parcel of the plaintiff's judgment in foreclosure. See *R.R. 4:55-8*.

When Congress directed that the government's lien under section 6321 "shall not be valid as against any mortgagee" it did not specifically spell out the elements of the mortgagee's claim entitled to priority. See 26 *U.S.C.A. § 6323*. But it seems entirely clear that at least principal, interest and costs were within the congressional contemplation. That much is not disputed by the government which set forth in its brief that here "the first and second mortgages were recorded before the federal tax lien was recorded and hence the principal and interest, plus costs of these mortgages are superior to the federal tax lien." And in a report submitted to this Court by the government following the sale of the foreclosed property it set forth the first mortgagee's priority as including principal, interest and taxed costs amounting to \$204.78. This latter sum consisted of filing fees, sheriff's fees and mileage, and \$50 under *N.J.S.A. 22A:2-10* for drawing pleadings plus \$100.78 search fees under *R.R. 4:55-9*. While the government excluded the sum of \$425.52 due the first mortgagee under *R.R. 4:55-7* (c), we fail to find any sensible basis for differentiating that item from the other items acknowledged by the government. Thus the \$50 item represents services by the plaintiff's attorney as might the \$100.78 item. Without impairing their true character as tra-

ditional and incidental costs, the state could readily and conveniently have provided for larger sums, by statutory or rule provision allowing individual amounts for each of the pleadings filed or each of the steps taken. In their aggregate these could well have exceeded those provided by the modest percentages fixed in *R.R. 4:55-7(c)* and, for present purposes, it would appear wholly immaterial which of these courses the State has chosen in dealing with its allowance of taxed costs.

The government continues its reliance on *Buffalo Savings, supra*, and *Pioneer, supra*, but these cases involved different situations. In *Buffalo Savings* the mortgage was executed in 1946, the government's lien was filed in 1953, and thereafter in 1957 and 1958 local liens for unpaid real estate taxes attached to the property. On foreclosure, the trial court directed that the local real estate taxes be paid as part of the expenses of sale prior to the satisfaction of the government's lien. This was reversed by the Supreme Court in a *per curiam* which pointed out that "the state may not avoid the priority rules of the federal tax lien by the formalistic device of characterizing subsequently accruing liens as expenses of sale." 374 U.S. at 229, 9 L.Ed.2d at 284. Here we are not dealing with any formalistic device or any circumvention of federal priority but with a traditional and incidental allowance by way of taxed costs for services which were truly part of the plaintiff's actual legal costs and expenses in foreclosing its mortgage. Indeed it may be assumed that its actual foreclosure expenses here exceeded its taxed costs. Its efforts in pursuing the foreclosure through sale have benefited not only the mortgagees but the government as well. In a fair sense, it has produced a fund from which the government will receive a return without any ex-

penditure on its own part. It would therefore appear that not only are the significant legal considerations unfavorable to the government's position here but so also are the equitable ones. See *Washington Const. Co. v. United States of America*, 75 N.J. Super. 536 (Ch.Div. 1962); *Smith v. Smith*, 78 N.J. Super. 28 (Ch.Div. 1963); but cf. *United States v. Pioneer American Ins. Co.*, *supra*, 374 U.S. at 92, 10 L.Ed. 2d at 777 n.13; *Camptown Savings & Loan Assn. v. United States, etc.*, 85 N.J. Super. 18, 20 (App.Div. 1964).

In *Pioneer* the holder of a note and mortgage instituted foreclosure proceedings in a state court. The note was in the face amount of \$20,000 and contained a provision that in the event of court proceedings the mortgagor would pay "a reasonable attorney's fee." The foreclosure decree fixed the attorney's fee at \$1250 and "after satisfaction of court and foreclosure sale costs" the mortgagee was accorded first priority for principal, interest and the attorney's fee. The Supreme Court, in holding that the federal tax lien under section 6321 was entitled to priority over the attorney's fee, found the latter to be inchoate rather than choate. See *Kennedy, The Relative Priority of the Federal Government: The Pernicious Career of the Inchoate and General Lien*, 63 Yale L.J. 905, 911 (1954); *Note, Federal Priorities & Tax Liens*, 63 Colum.L.Rev. 1259, 1264 (1963). Among other matters, it pointed to the fact that the mortgagee was obligated to pay a "reasonable" fee, that this related "to the service to be performed by the attorney," and that it could not be "finally fixed in amount" until the date of the decree. 374 U.S. at 87, 90-91, 10 L.Ed.2d at 773-774, 776.

Pioneer did not deal with any item of taxed costs allowed by statute or court rule but with a contractual agreement for the payment of a fee. Cf. *Bergen*

Builders, Inc. v. Horizon Developers, Inc. 44 N.J. 435 (1965). That contractual agreement provided, not for a fixed percentage as in *Security Mortg. Co. v. Powers*, 278 U.S. 149, 73 L.Ed. 236 (1928) (and as in our R.R. 4:55-7(c)), but for a reasonable fee which could not be ascertained until all of the legal work had been done and the final decree was about to be entered. While *Security Mortgage* dealt with a bankruptcy proceeding, it is to be noted that there Justice Brandeis remarked that "the lien was not inchoate" but "had already become perfect when the principal note and the loan deed serving it were given." 278 U.S. at 156, 73 L.Ed. at 241. See *United States v. Seaboard Citizens Nat. Bank*, 206 F.2d 62 (4th Cir. 1953).

The contours of the Supreme Court's doctrine of choateness remain to be fixed and undoubtedly further pronouncements by that Court will be handed down. See *United States v. Vermont*, 377 U.S. 351, 12 L.Ed.2d 370 (1964); *Kennedy, From Spokane County to Vermont: The Campaign of the Federal Government Against the Inchoate Lien*, 50 Iowa L. Rev. 724 (1965); compare *Streeter v. Overfelt*, 202 F.Supp. 143, 146 (D. Mont. 1962), with *First National Bank of Lewistown v. Tilzey*, 238 F.Supp. 750 (D. Mont. 1965). Nothing thus far, including *Pioneer* which contains no discussion whatever on the subject of taxed costs, persuades us that the traditional and incidental allowances in foreclosure proceedings under R.R. 4:55-7(c) are not lawfully and justly entitled to the same priority as that afforded to the mortgage principal and interest.

Reversed and remanded for distribution in conformity with the views expressed in this *per curiam*.

SUPREME COURT OF NEW JERSEY

Appeal Docket No. 4566

Civil Action
On Appeal

EQUITABLE LIFE ASSURANCE SOCIETY OF THE
UNITED STATES, PLAINTIFF-APPELLANT

vs.

ALBERT BAGIN, ET AL., DEFENDANTS-RESPONDENTS

Mandate on Reversal

This cause having been duly argued before this Court by Mr. Frank W. Hoak, counsel for the appellant and Mr. Edward J. Turnbach, counsel for the respondent, and the Court having considered the same.

It is hereupon ordered and adjudged that the judgment of the said Superior Court, Chancery Division is in all things reversed, set aside and for nothing holden, with costs;

and it is further ordered that this mandate shall issue ten days hereafter, unless an application for rehearing shall have been granted or is pending, or unless otherwise ordered by this Court, and that the record and proceedings be remitted to the said Superior Court, Chancery Division to be there proceeded with in accordance with the rules and practice relating to that court, consistent with the opinion of this Court.

WITNESS the Honorable JOSEPH WEINTRAUB,
Chief Justice, at Trenton on the 6th day of July,
1965.

/s/ John H. Gildea
Clerk
Clerk of the Supreme Court

A TRUE COPY

/s/ John H. Gildea
Clerk

FILED
JULY 6, 1965
John H. Gildea
clerk

SUPREME COURT OF NEW JERSEY

No. N-36 September Term 1965

EQUITABLE LIFE ASSURANCE SOCIETY,
PLAINTIFF-APPELLANT

VS.

ALBERT BAGIN, DEPENDANT-RESPONDENT

Motion for stay of mandate.

This matter having been duly considered by the Court, it is ORDERED that the mandate of this court issue with instructions that distribution be withheld of the sum of \$491.69 and that distribution be permitted of the conceded priority adjustment fund.

WITNESS the Honorable Joseph Weintraub, Chief Justice, at Trenton this twenty-first day of September 1965.

/s/ John H. Gildea
Clerk

A TRUE COPY

/s/ John H. Gildea
Clerk

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In the Supreme Court of the United States

OCTOBER TERM, 1965

No. 645

UNITED STATES, PETITIONER

v.

**THE EQUITABLE LIFE ASSURANCE SOCIETY OF THE
UNITED STATES**

**ON WRIT OF CERTIORARI TO THE SUPREME COURT OF THE
STATE OF NEW JERSEY**

BRIEF FOR THE UNITED STATES

OPINIONS BELOW

The opinion of the Superior Court, Chancery Division, Bergen County (R. 5-9), is not reported. The opinion of the Supreme Court of New Jersey (R. 13-19) is reported at 45 N.J. 206, 212 A.2d 25.

JURISDICTION

The judgment of the Supreme Court of New Jersey was entered on July 6, 1965 (R. 20). The petition for a writ of certiorari was filed on October 4, 1965, and was granted on January 17, 1966 (R. 22). The jurisdiction of this Court rests on 28 U.S.C. 1257(3).

QUESTION PRESENTED

A state law provides that, in mortgage foreclosure actions, an allowance for an attorney's fee, fixed as a percentage of the amount adjudged to be paid the mortgagee, shall be a part of the taxed costs of the action. The question presented is whether a federal tax lien is entitled to priority over the mortgagee's claim for such attorney's fee, where notice of the federal tax lien was recorded prior to default by the mortgagor.

STATUTES AND RULE INVOLVED

Sections 6321, 6322, and 6323 of the Internal Revenue Code of 1954 and Rule 4:55-7 of the Rules Governing the New Jersey Courts are set forth in the Appendix, *infra*, pp. 17-19.

STATEMENT

This case began as a mortgage foreclosure action brought by respondent, the first mortgagee. The mortgage, covering real property owned by Albert Bagin and his wife, had been executed on December 13, 1960, and recorded a few days later (R. 5). It secured the Bagins' indebtedness of \$30,000 to the respondent (R. 13-14). On March 21, 1962, a federal tax lien for \$7,748.91 was filed against Mr. Bagin (R. 5, 14). A year later he and his wife defaulted on the mortgage, and foreclosure proceedings were commenced in the Superior Court of Bergen County, Chancery Division (R. 2-3).

In the Chancery Division the United States admitted that its lien was subordinate to the principal

and interest on the two mortgages involved,¹ but claimed that its tax lien was superior to any claim for attorney's fees (R. 4, 6). The Chancery Court agreed and, in its decree of foreclosure, granted the federal tax lien priority over respondent's attorney's fees, which the court fixed under the State rules at \$425.52 (R. 8-11). Respondent appealed to the Superior Court of New Jersey, Appellate Division (R. 13). While the case was pending there, the appeal was certified to the New Jersey Supreme Court on the court's own motion (R. 14). That court directed that the property be sold forthwith, and after the sale ruled that the mortgagee's attorney's fee was payable ahead of the federal tax lien out of the proceeds of sale (R. 14-20).²

SUMMARY OF ARGUMENT

Under Sections 6321-6323 of the Internal Revenue Code, the United States receives a lien for unpaid taxes upon the property of the taxpayer which arises upon assessment. A judicial determination of the priority of the federal tax lien in relation to competing State-created liens must conform to the standards of federal law. Under the decisions of this Court, a recorded federal tax lien is subordinate to all prior, perfected liens and superior to all subse-

¹ A second mortgage had been recorded on December 19, 1960, and a third on May 18, 1961 (R. 5). A default judgment was entered against the third mortgagee (R. 5, 11).

² Under the Chancery Division's holding the United States was entitled to \$491.69 of the proceeds of sale. The holding of the Supreme Court of New Jersey effects a reduction of the share of the United States to \$66.17 (R. 15).

quent and inchoate liens. In *United States v. Pioneer American Ins. Co.*, 374 U.S. 84, those standards were applied with respect to a mortgagee's claim in a foreclosure suit for an award of attorney's fees based upon the mortgagor's undertaking, in the note and mortgage, to pay a reasonable attorney's fees in the event of foreclosure. The Court held that a federal tax lien arising and recorded after the commencement of the foreclosure suit was senior to the mortgagee's claim for attorney's fees which remained inchoate until reduced to judgment. In the present case, respondent's claim for attorney's fees is based upon Rule 4:55-7(c) of the Rules Governing the New Jersey Courts which provides an allowance for attorney's fees in foreclosure proceedings determined as a percentage of "all sums adjudged to be paid the plaintiff in such action". At the time that the federal tax lien was recorded—more than a year before default or foreclosure—respondent's potential claim was entirely contingent and indeterminate. Accordingly, the court below erred in subordinating the federal tax lien to respondent's claim for attorney's fees.

The court below held that, notwithstanding the decision in *Pioneer*, a State may subordinate a federal tax lien to a junior claim for attorney's fees by awarding the latter as part of the taxable costs of the foreclosure. It is well settled, however, that a State's characterization of State-created liens, while good for all State purposes, is not controlling in determining the standing of a federal tax lien. As this Court said in *United States v. Buffalo Savings Bank*, 371 U.S.

228, 229, "the state may not avoid the priority rules of the federal tax lien by the formalistic device of characterizing subsequently accruing local liens as expenses of sale." The characterization of attorney's fees as costs is a no less "formalistic device" to which the collection of federal revenues may not be subjected. While the United States has not challenged the award of costs generally, it has acted in light of the general rule in this country that attorney's fees are not taxable as costs. Its acquiescence, moreover, has been prompted by the fact that taxable costs in the usual case are *de minimis*, fixed in amount, and generally constitute reimbursement for sums paid over to State officials. The United States has not acquiesced in the subordination of federal tax liens to potentially substantial allowances for the counsel fees of adverse parties.

ARGUMENT

I. AS A MATTER OF FEDERAL LAW, RESPONDENT'S CLAIM FOR ATTORNEY'S FEES WAS INCHOATE WHEN THE FEDERAL LIEN AROSE AND IS THEREFORE SUBORDINATE TO SUCH LIEN

A. *The Relative Standing of a Federal Tax Lien is determined by Federal Law*

The Internal Revenue Code gives the United States a lien for unpaid taxes upon "all property and rights to property, whether real or personal" of the taxpayer; the lien arises when the assessment is made; but it is not valid against mortgagees, pledgees, purchasers or judgment creditors until it has been recorded (Sections 6321, 6322 and 6323 of

the Internal Revenue Code of 1954, Appendix, *infra*, pp. 17-19.)

The Court has long recognized that the uniform application of the federal laws and the protection of federal revenues require that State determinations of the relative priority of federal tax liens must meet federal standards.* "Otherwise, a State could affect the standing of federal liens * * * simply by causing an inchoate lien to attach at some arbitrary time * * *." *United States v. New Britain*, 347 U.S. 81, 86. It is therefore well established that, whatever may be the priorities among State-created liens, a recorded federal tax lien is subordinate to all prior, perfected liens and superior to all subsequent and inchoate liens.* Subsequently perfected liens do

* *United States v. Security Trust & Sav. Bank*, 340 U.S. 47, 49; *United States v. Gilbert Associates*, 345 U.S. 361; *United States v. Aciri*, 348 U.S. 211, 213.

* *Spokane County v. United States*, 279 U.S. 80; *New York v. Maclay*, 288 U.S. 290; *United States v. Waddill Co.*, 323 U.S. 353; *Illinois v. Campbell*, 329 U.S. 362; *United States v. Security Trust & Sav. Bank*, 340 U.S. 47; *United States v. New Britain*, 347 U.S. 81; *United States v. Aciri*, 348 U.S. 211; *United States v. Liverpool & London Ins. Co.*, 348 U.S. 215; *United States v. Scovil*, 348 U.S. 218; *United States v. Colotta*, 350 U.S. 808, reversing *per curiam*, 224 Miss. 33, 79 So. 2d 474; *United States v. White Bear Brewing Co.*, 350 U.S. 1010, reversing *per curiam*, 227 F. 2d 359 (C.A. 7); *United States v. Vorreiter*, 355 U.S. 15, reversing *per curiam*, 134 Colo. 543, 307 P. 2d 475; *United States v. Ball Construction Co.*, 355 U.S. 587, reversing *per curiam*, 239 F. 2d 384 (C.A. 5); *United States v. Hulley*, 358 U.S. 66, reversing *per curiam*, 102 So. 2d 599 (Fla.); *United States v. Buffalo Savings Bank*, 371 U.S. 228; *United States v. Pioneer American Ins. Co.*, *supra*; cf. *Crest Finance Co. v. United States*, 368 U.S. 347; *United States v. Vermont*, 377 U.S. 351.

not relate back to the time of their creation to defeat federal liens perfected in the interval.⁵ The underlying principle remains that stated by Chief Justice Marshall in *Rankin v. Scott*, 12 Wheat. 177, 179:

* * * [A] prior lien gives a prior claim, which is entitled to prior satisfaction, out of the subject it binds, unless the lien be intrinsically defective, or be displaced by some act of the party holding it * * *.

Clearly, departure from these guidelines would leave the status of federal tax liens to be "determined by the diverse rules of the various States" and result in the "unequal application of the federal tax laws, depending upon variances in the terms and phraseology of different state and local * * * statutes and judicial rulings thereon." *United States v. Speers*, 382 U.S. 266, 270-271.⁶

B. Respondent's Claim for Attorney's Fees was Indeterminate and Contingent when the Federal Tax Lien Arose

The United States conceded at the outset that the claims for the principal and interest under the mortgages had priority over the tax lien (R. 4). Respondent asserts that its claim for an attorney's fee, in an amount fixed by Rule 4:55-7(c) of the State court rules, is likewise entitled to priority. The decision below sustaining that assertion is completely at variance with the principles outlined above and the applicable decisions of this Court.

⁵ *United States v. Security Trust & Sav. Bank*, 340 U.S. 47, 50.

⁶ In each of the last three fiscal years the United States has been named as a party (under 28 U.S.C. 2410) in more than 4,800 actions to foreclose or quiet title affecting property on which it held liens.

When the tax lien was recorded on March 21, 1962, the mortgagor-taxpayer was meeting his obligations under the mortgage. It was not until March 1963 that he first defaulted, and it was not until June 1963 that respondent commenced foreclosure proceedings. (R. 2-3). The judgment of the Chancery Division was entered in April 1964. It follows that when the tax lien arose, respondent had no claim for attorney's fees, let alone a perfected lien for one. That claim remained a purely speculative contingency at least until default and the commencement of foreclosure proceedings.⁷ When the tax lien arose, respondent's potential claim under Rule 4:55-7(c) was not only indeterminate in amount but also appreciably further from perfection than "a *lis pendens* notice that a right to perfect a lien exists" (*United States v. Security Trust & Sav. Bank*, 340 U.S. 47, 50) and was barely a "*caveat* of a more perfect lien to come" (*New York v. Maclay*, 288 U.S. 290, 294).

The inchoate quality and subordinate standing of respondent's claim for attorney's fees was made abundantly clear in the Court's recent decision in *United States v. Pioneer American Ins. Co.*, 374 U.S. 84. *Pioneer* involved a mortgage which provided that a reasonable attorney's fee "shall be added to the principal sum * * * and shall be secured by this instrument" in the event of foreclosure (*id.* at 85 n. 1). The Court held that federal tax liens recorded after

⁷ Under Rule 4:82-5, a mortgagee who commences and then abandons a foreclosure action loses his claim to attorney's fees even though junior encumbrancers proceed with the action.

recordation of the mortgage, after default and after the initiation of a foreclosure suit, but before entry of a judgment fixing the amount of the attorney's fees, were entitled to priority over the claim for such fees. The Court regarded the mortgagee's claim for attorney's fees as similar to a lien to secure future indebtedness and, therefore, as inchoate as a matter of federal law. The court below (R. 18-19) sought to distinguish *Pioneer* in part on the ground that there the obligation to pay a reasonable fee could not be finally fixed in amount until the date of the decree whereas, in the present case, Rule 4:55-7(c) provides a precise method for determining the fee. The distinction is without substance because the fixed percentages which the rule specifies for determining the allowance are applied to "all sums adjudged to be paid the plaintiff in such [foreclosure] action" (Rule 4:55-7(c)). At the time the tax lien here arose there was no conceivable way of determining what sums or that any sum might someday be "adjudged to be paid the plaintiff." Therefore, here, as in *Pioneer*, the amount of the allowance could not be finally fixed until the date of the decree.*

* "That R.R. 4:55-7(c) sets forth the precise percentage which is to be allowed is also immaterial in the case at bar, for, when the federal tax lien was filed, the mortgage was not even in default. The amount of counsel fee could not become certain until after the mortgage fell into default, was foreclosed and the amount due the mortgagee (and the fee) was adjudged by the court." *Camptown Savings & Loan Assn. v. United States*, 85 N.J. Super. 18, 20-21 (App. Div.).

Moreover, the provision in *Pioneer* obligating the mortgagor to pay an attorney's fee was judicially enforceable only by virtue of a State statute which validated such agreements as

The only material differences between the facts of the present case and those in *Pioneer* tend to show that this case follows a *fortiori*, for Pioneer's claim was held inchoate notwithstanding the fact that,

* * * By the time the federal liens subordinated by the Arkansas courts were placed of public record, default had occurred, the mortgagee had elected to declare the note due and payable, an attorney had been engaged and a suit to foreclose the mortgage had been filed. [374 U.S. at 90.]

In the present case, all those events were over the horizon when the tax lien was recorded. Here, as in *Pioneer*, "a lien for an attorney's fee which is uncertain in amount and yet to be incurred and paid * * * is inchoate and is subordinate to the intervening federal tax lien filed before the mortgagee's lien for the attorney's fee matures" (*id.* at 91).

The court below (R. 19) relied on *Security Mortgage Co. v. Powers*, 278 U.S. 149, for the proposition that the fixed percentage feature of the attorney's fee in this case made the *Pioneer* rule inapplicable. In doing so it disregarded this Court's observation in *Pioneer* (374 U.S. at 90 n.8) that the issue in *Security* was the status of an attorney's fee clause in bankruptcy proceedings "where the rigorous federal lien choateness test was not necessarily applicable." In *Secu-*

contracts of indemnity and which limited such fee to 10 percent of the principal and interest due. 6A Ark. Stat. Anno. 68-910 (1957). Prior to the enactment of that statute, the Arkansas courts treated such agreements as unenforceable penalty provisions. See *Hollaway v. Pocahontas Federal Savings & Loan Ass'n*, 230 Ark. 310, 312, 323 S.W. 2d 204, 206.

ity, which did not involve the priority of a federal tax lien at all, the Court held that the validity of the lien claimed by the mortgagee for attorney's fees "must be determined" by State law (278 U.S. at 153); that the enforceability of the liability for attorney's fees against proceeds of the sale by the bankruptcy court raised "federal questions peculiar to the law of bankruptcy" (*id.* at 154); and that nothing in the Bankruptcy Act barred enforcement of the claim (*id.* at 155-160). Moreover, like *Pioneer*, but quite unlike the present case, in *Security* "the contingent obligation to pay attorney's fees was a part of the original transaction. The consideration for the lien was not the attorney's services, but the \$90,000 advanced by the Mortgage Company; and this was a present consideration." (*Id.* at 156). In sum, Security was found to have no bearing in *Pioneer* and it clearly has none here.

II. THE STATE CANNOT DEFEAT THE PRIORITY OF A FEDERAL TAX LIEN BY CHARACTERIZING THE ALLOWANCE OF ATTORNEY'S FEES AS AN AWARD OF COSTS

A. *The Standing of the Federal Tax Lien is not Determined by the State's Characterization of Competing Claims*

The *Pioneer* decision made it clear that a State's determination to enforce a mortgagor's agreement to pay the mortgagee's attorney's fees in foreclosure proceedings does not give a claim for such fees priority over an intervening federal tax lien. The court below held, however, that a State may achieve the same result by characterizing the allowance as part of the

costs of the foreclosure. Yet nothing is more clearly settled than that a State may not alter the standing of a federal tax lien by its characterization of competing State-created liens.

In *United States v. Acri*, 348 U.S. 211, 213, the Court said:

The relative priority of the lien of the United States for unpaid taxes is, as we said in *United States v. Waddill Co.*, 323 U.S. 353, 356, 357; *Illinois v. Campbell*, 329 U.S. 362, 371; *United States v. Security Trust Co.*, 340 U.S. 47, 49, always a federal question to be determined finally by the federal courts. The state's characterization of its liens, while good for all state purposes, does not necessarily bind this Court. *United States v. Waddill Co.*, 323 U.S. 353, at 357; *United States v. Gilbert Associates*, 345 U.S. 361.

The same principle was reiterated in *United States v. Buffalo Savings Bank*, 371 U.S. 228, where the Court held that a State could not give local real estate taxes priority over a federal tax lien by treating them as expenses of sale incurred in the foreclosure of a mortgage which was concededly senior to the federal lien—even though the burden of the State tax lien thereby fell upon the mortgagee. The Court there said (*id.* at 229) that “the state may not avoid the priority rules of the federal tax lien by the formalistic device of characterizing subsequently accruing local liens as expenses of sales.” Here priority has been conferred on a unmistakably junior claim by an equally “formalistic device.” A subordination of the federal lien which New York could not achieve under the rubric “expenses” and which Arkansas could not

achieve under the rubric "indemnity," New Jersey can not achieve under the rubric "costs."

To permit such a result would be to subject federal tax liens to the vagaries of purely arbitrary differences in the statutes, rules and decisions of the 50 states. Indeed, it would inevitably invite the States to overhaul the provisions for costs in their court rules.*

B. The Government's Concession of Costs to Senior Lienors does not Embrace Attorney's Fees

The fact that the United States has not contested the allowance of costs, not including counsel fees, to senior lienors can hardly constitute a concession with respect to the present claim. Because in the usual foreclosure proceeding, taxable costs are *de minimis*, fixed in amount, and generally constitute reimbursement for sums paid over to State officials, the United States has not challenged their award. But the decision not to do so has always been premised on the general rule in this country that attorney's fees are not taxable as costs.⁹

* Statutes in only three states now provide explicitly for an allowance of attorneys' fees as costs in foreclosures. 44 Iowa Code Anno. § 625.22; 7 Rev. Codes of Mont. § 93-8613; 46 Okla. Stat. Anno. § 56. A few other States provide for a judicial award of counsel fees without designating them as costs where, as in *Pioneer*, the contract imposes the obligation to pay such fees. See, e.g., VIII Conn. Gen. Stat. § 49-7; 4 Vt. Stat. Anno. § 4527.

⁹ See *Sprague v. Ticonic Bank*, 307 U.S. 161, 165-166; *Vaughan v. Atkinson*, 369 U.S. 527, 530; Barron and Holtzoff, *Federal Practice and Procedure*, Section 1197; 6 Moore, *Federal Practice and Procedure*, ¶ 54.77[2]; McCormick, *Counsel Fees and other Expenses of Litigation as an Element of Damages*, 15 Minn. L. Rev. 619 (1931).

As the Court wrote long ago in *Sioux County v. National Surety Co.*, 276 U.S. 238, 243-244, attorney's fees are not "costs in the ordinary sense of the traditional, arbitrary and small fees of court officers, attorneys' docket fees and the like * * *." This very distinction is well recognized in New Jersey. In *United States Pipe & Foundry Co. v. United Steelworkers of America*, 37 N.J. 343, 355-356, 181 A. 2d 353, 359, the New Jersey Supreme Court noted that costs generally "comprise principally certain statutory allowances, amounts paid the clerk in fees, and various other specified disbursements of counsel including sheriff's fees, witness fees, deposition expenses and printing costs. * * * Counsel fees, although if allowable are included in the taxed costs, are an entirely different matter."

Even in the present case the award for attorney's fees was more than twice the amount of all the other taxed costs; a larger mortgage would have produced a much greater discrepancy. Moreover, New Jersey might appreciably increase the percentage allowances now provided by Rule 4:55-7(c). The United States has not consented, and is certainly not obliged to consent, to the subordination of prior federal liens to potentially substantial claims for attorney's fees.¹¹ Nor is there any reason why federal liens should be so subordinated. Contrary to the suggestion of the court below (R. 18), this is not a case in which the efforts of counsel created a fund. Counsel did not bring an asset into being but merely liquidated one. It is not

¹¹ Among the costs to which the United States did not object below is an allowance (under N.J. Rev. Stat. 22A:2-10)

suggested that the attorney's services in any way increased the total amount available for distribution. Cf. *United States v. Hubbell*, 323 F. 2d 197 (C.A. 5). Moreover, as this Court said in *Pioneer* (374 U.S. 84, 92 n. 13), "The attorney's services * * * were rendered for the benefit of the mortgagee to protect his interest in the property, and the United States, holding an adverse interest, received no such benefit from them that its interest is to be charged therefor." Although New Jersey elects to characterize an allowance of attorney's fees as costs, there is no more reason here than in *Pioneer* to permit the State characterization to defeat the priority of the federal tax lien.

of \$50 for drawing pleadings. That allowance derives from a "very old provision * * * enacted at a time when there was little or no service of notices by mail, and contemplated the drawing of them in manuscript, copying them by hand, and the actual service of them on the respondents personally." *Steelman v. Moore Bros. Glass Co.*, 93 N.J. Eq. 533, 536, 117 A. 516, 517. Whether or not that small, fixed allowance should have been objected to as constituting an additional attorney's fee, failure to object cannot be considered as a concession with respect to attorney's fees generally.

CONCLUSION

The judgment of the Supreme Court of New Jersey should be reversed and the case remanded with directions to award priority to the federal tax lien over the claim for an attorney's fee.

Respectfully submitted.

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MARCH 1966.

APPENDIX

Internal Revenue Code of 1954:

SEC. 6321. LIEN FOR TAXES

If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, additional amount, addition to tax, or assessable penalty, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person.

(26 U.S.C. 1958 ed., Sec. 6321.)

SEC. 6322. PERIOD OF LIEN

Unless another date in specifically fixed by law, the lien imposed by section 6321 shall arise at the time the assessment is made and shall continue until the liability for the amount so assessed is satisfied or becomes unenforceable by reason of lapse of time.

(26 U.S.C. 1958 ed., Sec. 6322.)

SEC. 6323. VALIDITY AGAINST MORTGAGEES, PLEDGEES, PURCHASERS, AND JUDGMENT CREDITORS

(a) *Invalidity of Lien Without Notice.*—Except as otherwise provided in subsection (c), the lien imposed by section 6321 shall not be valid as against any mortgagee, pledgee, purchaser, or judgment creditor until notice thereof has been filed by the Secretary or his delegate—

(1) *Under state or territorial laws.*—In the office designated by the law of the State or Territory in which the property subject

to the lien is situated, whenever the State or Territory has by law designated an office within the State or Territory for the filing of such notice; or

(2) *With clerk of district court.*—In the office of the clerk of the United States district court for the judicial district in which the property subject to the lien is situated, whenever the State or Territory has not by law designated an office within the State or Territory for the filing of such notice; or

(3) *With clerk of district court for District of Columbia.*—In the office of the clerk of the United States District Court for the District of Columbia, if the property subject to the lien is situated in the District of Columbia.

(b) *Form of Notice.*—If the notice filed pursuant to subsection (a)(1) is in such form as would be valid if filed with the clerk of the United States district court pursuant to subsection (a)(2), such notice shall be valid notwithstanding any law of the State or Territory regarding the form or content of a notice of lien.

(c) *Exception in Case of Securities.*—

(1) *Exception.*—Even though notice of a lien provided in section 6321 has been filed in the manner prescribed in subsection (a) of this section, the lien shall not be valid with respect to a security, as defined in paragraph (2) of this subsection, as against any mortgagee, pledgee, or purchaser of such security, for an adequate and full consideration in money or money's worth, if at the time of such mortgage, pledge, or purchase such mortgagee, pledgee, or purchaser is without notice or knowledge of the existence of such lien.

(2) *Definition of security.*—As used in this subsection, the term “security” means any bond, debenture, note, or certificate or other evidence of indebtedness, issued by any corporation (including one issued by a government or political subdivision thereof), with interest coupons or in registered form, share of stock, voting trust certificate, or any certificate of interest or participation in, certificate of deposit or receipt for, temporary or interim certificate for, or warrant or right to subscribe to or purchase, any of the foregoing; negotiable instrument; or money.

(d) *Disclosure of Amount of Outstanding Lien.*—If a notice of lien has been filed under subsection (a), the Secretary or his delegate is authorized to provide by rules or regulations the extent to which, and the conditions under which, information as to the amount of the outstanding obligation secured by the lien may be disclosed.

(26 U.S.C. 1958 ed., Sec. 6323.)

Rules Governing the New Jersey Courts (1965 ed.):

4:55-7. *Counsel Fees*

No fee for legal services shall be allowed in the taxed costs or otherwise, except:

* * * *

(c) In an action for the foreclosure of a mortgage. The allowance shall be calculated as follows: on all sums adjudged to be paid the plaintiff in such an action, amounting to \$5,000 or less, at the rate of 3%, provided, however, that in any action a minimum fee of \$75 shall be allowed; upon the excess over \$5,000 and up to \$10,000 at the rate of 1½%; and upon the excess over \$10,000 at the rate of 1%.

* * * *

FILED

APR 8 1966

JOHN R. DAVIS, CLERK

Supreme Court of the United States

OCTOBER TERM, 1965

No. 646

UNITED STATES,

Petitioner,

vs.

THE EQUITABLE LIFE ASSURANCE SOCIETY
OF THE UNITED STATES,

Respondent.

On Writ of Certiorari to the Supreme Court of the
State of New Jersey

BRIEF AND APPENDIX FOR RESPONDENTS

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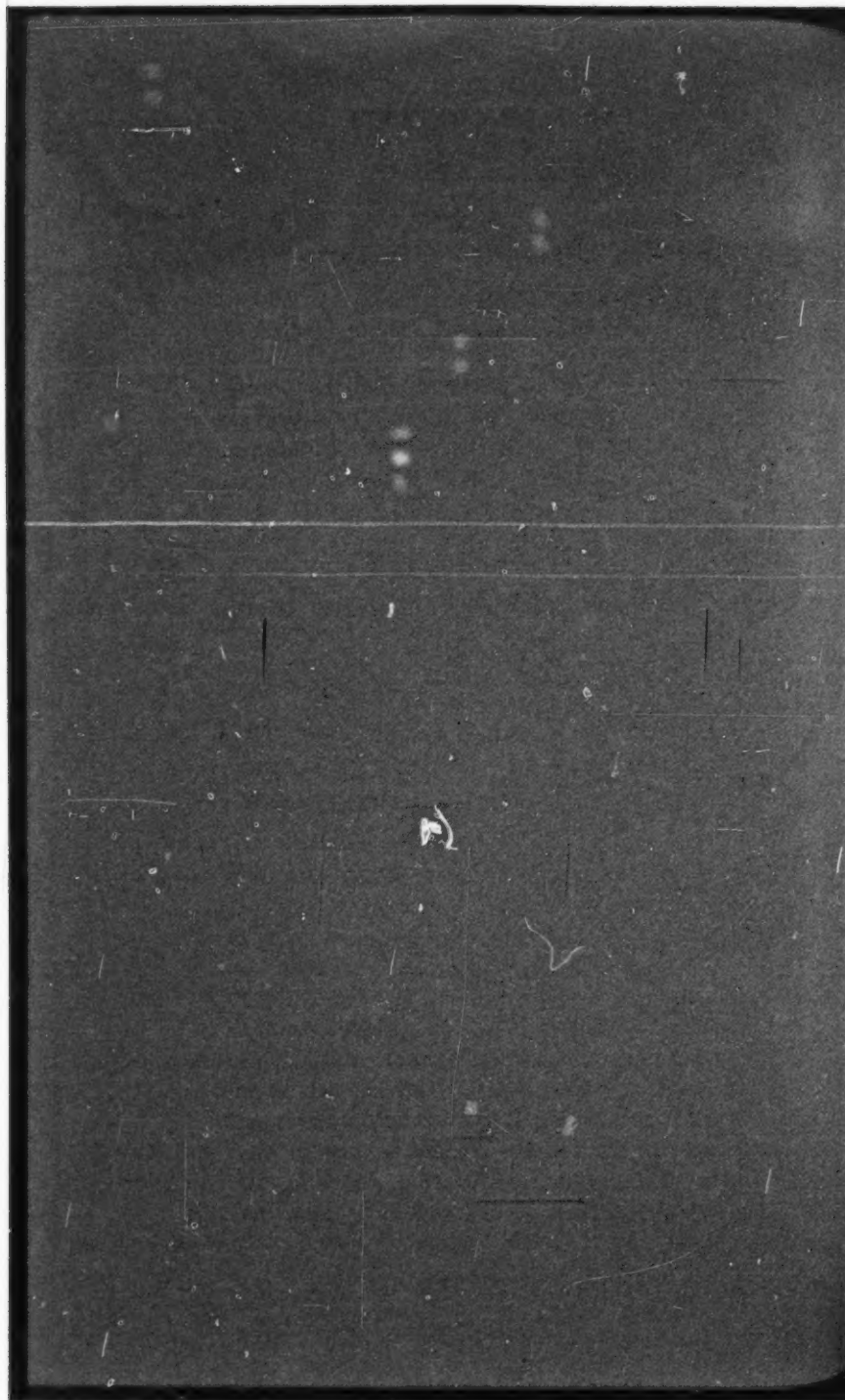


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IN THE
Supreme Court of the United States

OCTOBER TERM, 1965

No. 645

UNITED STATES,

Petitioner,

v.

THE EQUITABLE LIFE ASSURANCE SOCIETY OF THE
UNITED STATES,

Respondent.

On Writ of Certiorari to the Supreme Court of the
State of New Jersey

BRIEF FOR RESPONDENTS

Counter-Statement of Questions Presented

The specific question raised in this case is whether a foreclosing mortgagee in New Jersey is entitled to receive out of the proceeds of sale of the mortgaged premises the amount of the counsel fee allowed under R.R. 4:55-7 (c) before payment is made to the United States on account of

a tax lien that was recorded more than two years after the mortgage and about one year before the default that resulted in the foreclosure action and sale. Although this specific question appears at first blush to be very narrow, the ramifications that are involved in the reasoning that the court chooses to apply in reaching its decision lead to the *real question* that is involved, viz.:

What is the scope of the protection that Congress has given to mortgagees when the statutory provision of 26 U. S. C. §6323 (a) that a federal tax lien "shall not be valid as against any mortgagee * * * until notice thereof has been filed" is interpreted in the light of the "choateness rule" created by this court.

Summary of Argument

Mortgagees are presently being denied the protection Congress intended to give them in 1913, because this court has not defined the "choateness rule" as it applies to mortgagees. Since the advent of the "choateness rule" into the field of non-insolvency cases, every mortgage foreclosure action known to respondents that involves a federal tax lien becomes a contested action, in which the United States "disputes the priority of counsel fees and of any advances whatsoever made after the assessment dates of the lien of the United States."

Mortgagees can be relieved of this burden of contested foreclosure actions, and can again receive the protection Congress intended them to have, if this court will decide the choateness of the counsel fee in New Jersey foreclosure actions upon the basis of a principle that can be applied to every right held by a mortgagee, stated in such clear terms that reasonable men cannot differ as to the result.

Respondents suggest the following definition:

If the amount of the item in question can be determined at the moment the notice of federal tax lien is filed, without making any assumptions other than (1) a date to which interest is to be computed, and (2) that if the mortgagor had defaulted, his default was in payment of the item in question, that item constitutes a "choate lien" and is entitled to priority over the federal tax lien, it being immaterial whether or not the mortgagor has actually defaulted.

ARGUMENT

POINT I

Mortgagees are presently denied the protection Congress intended to give them because this Court has yet to define the "choateness rule" as it applies to a mortgagee.

Respondents recognize, as did the Supreme Court of New Jersey, that the effect of a lien in relation to a provision of federal law for the collection of debts owing to the United States is always a federal question, to be decided ultimately by the Supreme Court of the United States. Of the many cases decided by this court in the broad field of competition between state-created liens and federal tax liens, however, none has involved a situation comparable to that in the present case. The efforts of the petitioner to bring this case within the scope of the decisions in *United States v. Pioneer American Ins Co.*¹ and

¹ 374 U. S. 84, 10 L. Ed. 2d 770, 83 S. Ct. 1651 (1963).

United States v. Buffalo Savings Bank,² if successful, would produce a holding either that could not be applied uniformly or that would almost completely emasculate the protection given to mortgagees by Congress in 1913.

In order to focus attention upon the basic principles involved in this case, it will be helpful to assume that the competition is directly and solely between the foreclosing first mortgagee and the United States. The second mortgage, which was given by the mortgagors on the same date as the first mortgage, merely increases the size of the priority adjustment fund which the United States has conceded is to be distributed according to state law (RA2a).

Commencing in 1866, Congress has provided that if any person liable to pay any tax neglects or refuses to pay the same after demand, the amount, with certain additions, "shall be a lien in favor of the United States upon all property, whether real or personal, belonging to such person."³ In 1893 this court determined that this tax lien, though secret, was good even against a purchaser for value without notice.⁴ However, Congress changed the law as to mortgagees, purchasers, and judgment creditors in 1913, and as to pledgees in 1939. With respect to mortgagees, it provided that this tax lien "shall not be valid as against any mortgagee * * * until notice thereof has been filed by the Secretary or his delegate."⁵ It is this provision that

² 371 U. S. 228, 9 L. Ed. 2d 283, 83 S. Ct. 314 (1963).

³ July 13, 1866, c. 184, §9, 14 Stat. 107; R.S. §3186(a); I. R. C., 1939, §3670; I. R. C., 1954, §6321, 26 U. S. C. §6321.

⁴ *United States v. Snyder*, 149 U. S. 210, 37 L. Ed. 705, 13 S. Ct. 846 (1893).

⁵ R.S. §3186 (b); I. R. C., 1939, §3672; I. R. C., 1954 §6323; 26 U. S. C. §6323.

must be interpreted and delimited in the present case.

The Congressional acts have not spelled out the details of the protection intended to be given to a mortgagee, and there has always been doubt concerning the priority of a federal tax lien in relation to any item involved in the lien held by a mortgagee that the United States has chosen to contest.

This court began to bring some order into the general field of competition between state-created liens and federal tax liens when, in 1950, it first applied the "choateness rule" to a non-insolvency case.⁶ Unfortunately, this single event marked the end of the protection which Congress intended to give to mortgagees, for now every mortgage foreclosure action that involves a federal lien, whether it be for taxes or for a lien such as a mortgage, becomes a contested action, in which the United States picks certain items and disputes their priority. In most cases the mortgagees have capitulated, because of the expenses involved in an appeal on which this court is the final arbiter.

The reason for this unfortunate state of affairs was well stated by the Supreme Court of New Jersey in its opinion in this case: "The contours of the Supreme Court's doctrine of choateness remain to be fixed and undoubtedly further pronouncements by that Court will be handed down." (Tr. 19).

Until this court has clearly defined the "choateness rule" as it applies to a mortgagee, however, the mortgagee is utterly helpless because the United States, as indicated in its brief in this case, selects certain items to contest,

⁶ *United States v. Security Trust and Savings Bank*, 340 U. S. 47, 5 L. Ed. 53, 71 S. Ct. 111 (1950).

without considering the underlying principles involved.⁷ Under such circumstances, the mortgagee is not protected, as Congress intended, but is continually subjected to contested foreclosure actions with no reasonable hope for relief other than imploring this court to decide this case on the basis of the principles involved, so that the minds of reasonable men can no longer differ when the "choateness rule" is applied to any element of a mortgage lien.⁸

Before an acceptable statement of the "choateness rule" as applied to a mortgagee can be formulated, however, it is necessary to examine and define two things, *viz.*, the "cho-

⁷ Throughout its brief, the United States gives evidence of the predicament of mortgagees in recent years. "The United States has not acquiesced in the subordination of federal tax liens to potentially substantial allowances for the counsel fees of adverse parties" (Pb5). "The United States conceded at the outset that the claims for principal and interest under the mortgages had priority over the tax lien" (Pb7). "The fact that the United States has not contested the allowance of costs, not including counsel fees, to senior lienors can hardly constitute a concession with respect to the present claim. Because in the usual foreclosure proceeding, taxable costs are *de minimis*, fixed in amount, and generally constitute reimbursement for sums paid over to State officials, the United States has not challenged their award" (Pb13). "The United States has not consented, and is certainly not obliged to consent, to the subordination of prior federal liens to potentially substantial claims for attorney's fees" (Pb14).

⁸ For years mortgagees, as well as other lienholders, such as mechanic's lien claimants who are not protected by the 1913 Congressional act, have sought relief in the Congress. Unfortunately, the Congress moves slowly and cautiously in such matters. Note that it took 20 years after this court had decided the *Snyder* case until Congress acted to protect mortgagees, purchasers, and judgment creditors, and 46 years until it acted to protect pledgees.

ateness rule", and the rights of the mortgagee. They will be examined in that order.

A. The "Choateness Rule"

The "choateness rule" was formulated in a line of cases involving situations in which the taxpayer was insolvent. Since before 1800 Congress has provided that in such circumstances "the debts due to the United States shall be first satisfied."⁹ Although none of the statutes embodying this provision has contained any exceptions, language used in some of the earliest cases has resulted in many efforts to have this court declare that an exception does exist in the case of a competing lien that was "fully perfected and specific" prior to the insolvency. However, the court has never found it necessary to determine whether the exception actually does exist, because it has never decided a case in which the competing lien was found to be "fully perfected and specific prior to the insolvency." None of the decisions has involved competition between a federal tax lien and a mortgage on real property. Therefore, this line of cases is not at all helpful in determining the scope of the protection which Congress has given to mortgagees since 1913.

Furthermore, in *United States v. Vermont*,¹⁰ this court rejected the contention of the United States "that federal tax liens are entitled to priority * * * over any antecedent lien which is not sufficiently perfected to prevail against the explicit priority which R.S. §3466 gives to claims of

⁹ March 3, 1797, c. 20, §5; 1 Stat. 515; R. S. §3466; 31 U. S. C. §191.

¹⁰ 377 U. S. 351, 12 L. Ed. 2d 370, 84 S. Ct. 1267 (1964).

the United States in situations involving insolvency."¹¹ The Court stated that the *New Britain* case, which did not involve an insolvency situation, "makes quite clear that different standards apply where the United States' claim is based on a tax lien arising under §§6321 and 6322",¹² and that the argument of the United States "fails to discriminate between the standards applicable under the federal tax lien provisions and those applicable to an insolvent debtor under R.S. §3466." ^{11 13}

The first tax lien case in which this court applied the "choateness rule" was *United States v. Security Trust and Savings Bank*, decided in 1950.¹⁴ The case involved competition between a California attachment lien and three federal tax liens, notices of which were filed about two months after the attachment and about four months before judgment was entered in the attachment action. The attachment lien was held to be contingent or inchoate under both state and federal law.

The same result was reached in *United States v. Acri*,¹⁵ even though under state law an Ohio attachment lien is deemed to be perfected at the time of the attachment, and in *United States v. Liverpool & London & Globe Ins. Co.*,¹⁶ which involved garnishment of insurance proceeds.

¹¹ 377 U. S. at 356; 12 L. Ed. 2d at 374.

¹² 377 U. S. at 358; 12 L. Ed. 2d at 375.

¹³ Hereafter when reference is made to "tax lien cases", the cases do not involve an insolvent taxpayer. The phrase "tax lien cases" is used to distinguish such cases from "insolvency cases."

¹⁴ 340 U. S. 47, 95 L. Ed. 53, 71 S. Ct. 111 (1950).

¹⁵ 348 U. S. 211, 99 L. Ed. 264, 75 S. Ct. 239 (1955).

¹⁶ 348 U. S. 215, 99 L. Ed. 268, 75 S. Ct. 247 (1955).

From the standpoint of the present case, the most significant fact involved in these attachment and garnishment cases is that the lien in competition with the federal tax lien was not held by a "mortgagee, pledgee, purchaser, or judgment creditor", and thus there was no Congressional act giving such liens priority over unrecorded federal tax liens. Justice Jackson, concurring in the *Security Trust* case, stated that: "The history of this tax lien statute indicates that only a judgment creditor in the conventional sense is protected";¹⁷ and, with two justices dissenting, the court adopted this statement in *United States v. Gilbert Associates*.^{18 19} In that case, the New Hampshire Supreme Court had stated that "It is settled by our decisions that the assessment of a tax is in the nature of a judgment, enforced by a warrant instead of an execution."²⁰ This court held, however, that "Congress used the words 'judgment creditor' in §3672 in the usual, conventional sense of a judgment of a court of record".²¹

In succeeding cases, this court has developed the principle of these cases into a very important guidepost. Thus, in

¹⁷ 340 U. S. at 52; 95 L. Ed. at 57.

¹⁸ 345 U. S. 361, 97 L. Ed. 1071, 73 S. Ct. 701 (1953).

¹⁹ Although the taxpayer in *Gilbert Associates* was insolvent, this court first considered the status of the municipality as "a judgment creditor within the meaning of §3672". After rejecting the claim of the municipality on this ground, the court went on to consider and reject its claim as the holder of a general lien on all the taxpayer's property, the decision on this point being based upon the priority given to the United States when the taxpayer is insolvent, at least where the state-created lien is not "a perfected and specific lien."

²⁰ 345 U. S. at 363, 97 L. Ed. at 1075.

²¹ 345 U. S. at 364, 97 L. Ed. at 1075.

United States v. Scovil,²² which involved a landlord's distress for rent that was commenced after several federal tax liens had arisen, but before notice of the tax liens had been filed, the court held that the landlord obviously was not a purchaser, stating that: "A purchaser within the meaning of §3672 usually means one who acquires title for a valuable consideration in the manner of vendor and vendee".²³ It also held that the United States must prevail on its tax liens because: "The landlord had a lien other than a mortgage, pledge, or judgment lien. As to all other liens, such as the distress lien in the instant case, §3672 of the Internal Revenue Code affords no protection."²⁴ In *United States v. New Britain*,²⁵ which is discussed hereafter, the court stated that: "There is nothing in the language of §3672 to show that Congress intended antecedent federal tax liens to rank behind any but the specific categories of interests set out therein, and the legislative history lends support to this impression."²⁶

The full significance of these holdings in *Security Trust, Gilbert Associates, Scovil*, and *New Britain*, is brought out in *United States v. White Bear Brewing Co.*,²⁷ which is one of a series of four cases involving mechanic's liens, each of which resulted in a *per curiam* reversal by this court of decisions which had given priority to the mechanic's lien. In the other three cases, even though the mechanic's liens had arisen under the applicable state statutes prior to the

²² 348 U. S. 218, 99 L. Ed. 271, 75 S. Ct. 244 (1955).

²³ 348 U. S. at 220, 99 L. Ed. at 274.

²⁴ 347 U. S. 81, 98 L. Ed. 520, 74 S. Ct. 367 (1954).

²⁵ 347 U. S. at 88, 98 L. Ed. at 527.

²⁶ 350 U. S. 1010, 100 L. Ed. 871, 76 S. Ct. 646 (1956).

filing of the notices of federal tax liens, the actions to enforce the state-created liens were not commenced until after the federal notices had been filed. In *White Bear*, however, two justices dissented on the ground that "the mechanic's lien was specific, prior in time, perfected in the sense that everything possible under state law had been done to make it choate, and was being enforced before the federal tax lien arose. * * * The contract had been performed, the mechanic's lien recorded for a specific amount, and suit instituted to enforce the lien—all before the federal taxes were assessed and the tax liens recorded. Moreover, by the time the United States filed the present action to foreclose its tax liens, the mechanic's lien had been reduced to judgment, and the real estate sold at public auction and transferred by the purchaser to others."²⁷

Interpreting the result of the *White Bear* case in the light of the prior holdings of this court, we find that Congress had provided no protection from a federal tax lien to any lien claimant who is not a mortgagee, pledgee, purchaser, or judgment creditor. Therefore, in order for a lien claimant such as the holder of a mechanic's lien to prevail over a federal tax lien, it is necessary for the lien claimant to have achieved the status of a judgment creditor "in the usual, conventional sense of a judgment of a court of record," prior to the time notice of the federal lien is recorded.

Further guideposts are found in *United States v. New Britain*, *supra*,²⁸ and *United States v. Buffalo Savings Bank*.²⁹ The principal contributions of *New Britain* are its definition of a "choate lien" as one in which "the identity

²⁷ 350 U. S. at 1010, 100 L. Ed. at 871.

²⁸ 347 U. S. 81, 98 L. Ed. 520, 74 S. Ct. 367 (1954).

²⁹ 371 U. S. 228, 9 L. Ed. 2d 283, 83 S. Ct. 314 (1963).

of the lienor, the property subject to the lien, and the amount of the lien are established"³⁰ and its statement that the priority of a lien created by state law in relation to a federal tax lien "must depend on the time it attached to the property in question and became choate".³¹ In any discussion of *New Britain*, it is important to bear in mind that the dispute was between the United States with its tax liens and the City of New Britain with its liens for delinquent real estate taxes and water rents. The dispute involved surplus moneys in a mortgage foreclosure action, after the two mortgages held by the plaintiff had been paid in full, together with all expenses of sale, including attorney's fees for the foreclosure action. The holding was that the municipal tax liens, even though given priority over the mortgages by state law, were not entitled to priority over the federal tax liens unless they had attached to the property and become choate prior to the time at which the federal tax liens arose.³² As noted above, the court had previously determined in *United States v. Gilbert Associates*,³³ that Congress had provided no priority for municipal tax liens that attach after federal tax liens have arisen unless the municipality has achieved

³⁰ 347 U. S. at 84, 98 L. Ed. at 525.

³¹ 347 U. S. at 86, 98 L. Ed at 526.

³² It appears that the federal tax liens arose after some of the municipal liens had attached to the property and become choate but before other municipal liens had attached and become choate. The ultimate distribution on remand did not make a distinction, however, because the United States was paid in full and the City received the other available funds and also the balance due to it at the expense of a judgment creditor, pursuant to state law. *Brown v. General Laundry Service, Inc.*, 19 Conn. Sup. 335, 113 A. 2d 601 (Super. Ct. 1955).

³³ 345 U. S. 361, 97 L. Ed. 1071, 73 S. Ct. 701 (1953).

the status of a "judgment creditor" prior to the time that notice of the federal tax liens is filed.³⁴ The court specifically bypassed the question of whether the mortgagee could have advanced the delinquent taxes and water rents pursuant to the terms of the mortgage and claimed priority for these advances as part of the mortgage, because the mortgagee had not made any such advancements.³⁵ Thus, there is nothing in *New Britain* other than the definition of choateness that helps us determine the scope of the protection which Congress afforded to mortgagees as to any portion of its mortgage lien that, from the inception of the mortgage, is an integral part of the lien.

*Buffalo Savings Bank*³⁶ also involved delinquent real estate taxes and delinquent sewer and water rents, all of which accrued after notice of a federal tax lien had been filed. The New York Court of Appeals,³⁷ with two judges dissenting, had held that the foreclosing mortgagee and the municipality had liens which "attached directly to the particular parcel of real property" while the federal lien arose "because of an unconnected indebtedness of the owner of

³⁴ In *New Britain*, the court distinguishes *Gilbert Associates* on the ground that "the question we have here did not arise there because that was a case involving personal property and insolvency of the taxpayer". (347 U. S. at 87, 98 L. Ed. at 526). The remark does not detract from the first holding in *Gilbert Associates* that the municipality could only be a judgment creditor under §3672 if it were a judgment creditor "in the usual, conventional sense of a judgment of a court of record." (345 U. S. at 364, 97 L. Ed. at 1075).

³⁵ 347 U. S. at 87, 98 L. Ed. at 527.

³⁶ 371 U. S. 228, 9 L. Ed. 2d 283, 83 S. Ct. 314 (1963).

³⁷ *Buffalo Savings Bank v. Victory*, 11 N. Y. 2d 31, 226 N. Y. S. 2d 382, 181 N. E. 2d 413 (1962).

the land" and was filed "against a presumed equity in the real property held by the mortgagor" which would have substance only if a sale of the property should produce a surplus after payment of all liens such as the mortgage and the tax, sewer and water liens for essential services, in which "the property itself, in its very nature as land, incurs the indebtedness".³⁸ Based upon this property concept,³⁹ the state court decreed that the delinquent real estate taxes and sewer and water rents should be paid, pursuant to state law and practice, "out of the proceeds of the sale as expenses of the sale", with the federal tax lien attaching to any surplus.⁴⁰

With one dissent, this court reversed the state court, commenting that "the state may not avoid the priority rules of the federal tax lien by the formalistic device of characterizing subsequently accruing local liens as expenses of sale".⁴¹

The decision in *Buffalo Savings Bank* is consistent with that in *New Britain*, in which the court, while giving priority to municipal liens that had accrued prior to the time the federal tax liens had arisen, refused to give priority to the municipal liens that accrued thereafter. As in *New Britain*, the court was not called upon to consider what the result

³⁸ 11 N. Y. 2d at 38 and 39, 226 N. Y. S. 2d at 387.

³⁹ In the discussion of mortgages which follows, it will be apparent that the property concept was properly rejected by this court, and respondents in the present case make no such claim.

⁴⁰ 11 N. Y. 2d at 43, 226 N. Y. S. 2d at 391.

⁴¹ 371 U. S. at 229, 9 L. Ed. 2d at 284.

would have been if the mortgagee had advanced the municipal taxes, sewer rents, and water rents pursuant to the terms of the mortgage, with the amount so advanced becoming part of the mortgage debt covered by the mortgage. Since the state-created liens in question were not in existence at the time the notices of federal tax liens were filed, and hence were clearly inchoate by federal standards, *Buffalo Savings Bank* establishes only that the state cannot transform these inchoate liens into choate liens by making them a part of the expenses of sale and, in effect, a part of the mortgage lien. Municipal tax liens are not a part of a mortgage lien unless the mortgagee has advanced money pursuant to the terms of the mortgage to pay the taxes, and whether or not the amounts of its advancements will be choate or inchoate liens depends upon whether the municipal taxes being paid are choate or inchoate. The decision in *Buffalo Savings Bank* does not apply to items which are integral parts of the original mortgage lien.

Finally, in *United States v. Pioneer American Insurance Company*⁴² this court rejected the "contention that the choateness rule has no place when a mortgage under §6323 (a) is involved",⁴³ stating that "we believe Congress intended that if out of the whole spectrum of state-created liens, certain liens are to enjoy the preferred status granted by §6323, they should at least have attained the degree of perfection required of other liens and be choate for the purposes of the federal rule. The Court has never held that mortgagees face a less demanding test of perfection than other interests when competing with the federal lien."^{43 44}

⁴² 374 U. S. 84, 10 L. Ed. 2d 770, 83 S. Ct. 1651 (1963).

⁴³ 374 U. S. at 89, 10 L. Ed. 2d at 775.

⁴⁴ The holding of the court that the reasonable counsel fee in *Pioneer* was inchoate will be discussed later in the brief.

B. The Rights of the Mortgagee

A mortgagee is defined as a person to whom property is mortgaged, while a mortgage is a conveyance of property as security for the payment of a debt.⁴⁵ A security is "an instrument which renders certain the performance of a contract".⁴⁶

The first thing to be noted about a mortgage, then, is that it is needed only if there is a default in the performance of some other contract. In the usual case involving land, it renders certain the performance of a borrower under the terms of a bond or a note. So long as the borrower lives up to his obligations on the bond or the note, the mortgage is of no benefit to the mortgagee. His rights under the mortgage become meaningful only if and when the borrower, or mortgagor, defaults in his obligations under the bond or note.

The history of mortgages, which are of very ancient origin,⁴⁷ shows that the rights of the mortgagee, in the event of a default by the mortgagor in his principal obligation, have varied from time to time.

The common law conception of a mortgage was a conveyance of the legal title upon condition in the nature of a defeasance, *i.e.*, the payment of the debt on the very day stipulated. In default of strict compliance with the condition, the conveyance *ipso facto* became absolute and the mortgagee's

⁴⁵ Webster's New Collegiate Dictionary (2d ed., 1953) 549.

⁴⁶ Bouvier's Law Dictionary (Baldwin's Century Edition, 1929) 1098.

⁴⁷ The Bible speaks of persons who mortgaged their lands, vineyards and houses to buy grain because of a famine and to pay the king's taxes. *Nehemiah* V. 3, 4.

estate ripened into an indefeasible legal title in consonance with the terms of the conveyance.⁴⁸

Equity very early took jurisdiction to grant relief from such forfeitures if it could find equitable grounds, for example, where payment had been prevented by the mortgagee or by accident. By the year 1625, equity considered that the real nature of a mortgage transaction was a debt (the principal obligation) and it took jurisdiction to decree that the forfeiture of the land could be relieved by the *payment of the debt, with interest, expenses, and costs*, without considering the reason for the default. This redeemable interest was designated as the equity of redemption, since it could be enforced only in the courts of equity, and this equity developed into an estate in land which could be devised, granted, or entailed.⁴⁹

Having provided protection to the mortgagee through the equity of redemption, it was found to be necessary to provide some protection for the mortgagor, because it was deemed unreasonable to permit the mortgagor, or one holding under or through him, to come in to redeem at any time. Thus, in about 1629, the Court of Chancery enabled the mortgagee to file a bill for an account and to obtain a decree that the mortgagor or those claiming under or through him pay *the sum due, with interest and costs*, within a reasonable time, or be foreclosed of the equity of redemption. This procedure, known in this country as strict fore-

⁴⁸ *Scars, Roebuck & Co. v. Camp*, 124 N. J. Eq. 403, 407, 1 A. 2d 425, 427 (E. & A. 1938).

⁴⁹ It is this concept of the equity of redemption as an estate in land that forms the basis of the rejection of the property concept relied upon by the New York Court of Appeals in *Buffalo Savings Bank*.

closure, was the usual practice in New Jersey in colonial days, and was available as a means of cutting off the equity of redemption of mortgagors until 1880.

Many courts felt that strict foreclosure was too severe, however, in that the equity of redemption might be barred even though the value of the property was in excess of the mortgage debt, and because of the general acceptance of the theory that the mortgagee does not obtain a "conveyance of the legal title upon condition in the nature of a defeasance", but rather a lien upon the property, i.e., a security interest therein. Either with or without statutory authority, courts began to order judicial sales of the property, rather than strict foreclosure, and today in this country foreclosure by sale is employed almost universally, although in a few states strict foreclosure or powers of sale contained in the mortgages are still recognized.

The first statute relating to sale of the mortgaged premises in New Jersey appeared in 1772. It provided for service of process by publication on absconding mortgagors, or on mortgagors who refused to appear. Upon the expiration of the time limited by the order, and proof of publication and posting, a decree *pro confesso* might be entered and a sale by the sheriff ordered. The statute, which was probably copied from a New York statute of 1760, was re-enacted several times, but has existed in its present form, with only minor amendments, since 1873. Although strict foreclosure existed as an alternative remedy in the early days, the courts did not hesitate to order a sale under their inherent equity jurisdiction, especially in the case of infants; and long before 1880, when foreclosure by execution

sale became mandatory in New Jersey, it was the customary form of relief granted to the mortgagee.⁵⁰

Thus, in 1913, when Congress provided that a federal tax lien should be invalid as to any mortgagee until notice is filed, it must have been aware that a mortgagee in New Jersey, and in most other states, had no right to take any action under its mortgage unless and until the mortgagor defaulted in his obligations to repay the indebtedness secured by the mortgage. It must also have been aware that the only way in which the mortgagor could avoid foreclosure of his equity of redemption, from the time the equity of redemption was first created by the English courts of chancery, was to pay the *sum due, with interests and costs*. It must also have been aware that a mortgage is made up of several parts—principal, interest, additional advances of principal, advances to pay delinquent taxes, advances to pay delinquent insurance premiums, advances to make necessary repairs, and the costs involved in realizing these sums out of the mortgaged property. These costs include: the cost of searches needed to determine the parties affected by a foreclosure action; filing fees for complaint and notice of *lis pendens*; sheriff's fees and/or publication fees for making service; advertising fees in connection with the sheriff's sale; sheriff's disbursements for conducting the sale and conveying the property to the purchaser; sheriff's commissions on the sale; and the fees of the attorney who conducts the foreclosure action.

⁵⁰ Tischler, *Strict Foreclosure in New Jersey*, 64 N. J. L. J. 141, 145 & 146 (3-27-41). The article, written by one of New Jersey's leading lawyers and teachers in the field of real property, contains substantial citations of authorities for the propositions stated from footnote 48 to footnote 50.

Congress must be presumed, therefore, to have intended to protect each and every one of these elements of a mortgage when it made an unrecorded federal tax lien invalid as to *mortgagees*. This court has not declared anything different. It has merely stated that Congress intended to give priority over the federal tax lien only if the competing state-created lien meets the federal "choateness rule". We must turn, then, to an examination of the various elements of a mortgage lien in the light of this court's development of the "choateness rule" in the tax lien cases.

C. The "Choateness Rule" applied to the Rights of the Mortgagee

The United States includes several statements in Point I, A of its brief which it denominates "guidelines" to be applied in determining the priority of state-created liens and federal tax liens (Pb5-7). The difficulty, however, is that these co-called guidelines include such words as "liens", "prior, perfected liens", "inchoate liens", and "subsequently perfected liens", and the brief of the United States does not include a discussion of the principles to be applied in defining these terms. Instead, because a counsel fee was denied priority in *Pioneer*, the United States believes that all counsel fees must be denied priority, and that it is not necessary to define the "choateness rule" in relation to a mortgagee to any greater extent. It argues, citing *United States v. Speers*,⁵¹ that there can be no "unequal application of the federal tax laws, depending upon variances in the terms and phraseology of different state and local *** statutes and judicial rulings thereon" (Pb7). The fact is, however, that Congress provided for

⁵¹ 382 U. S. 266, 15 L. Ed. 2d 314, 86 S. Ct. 411 (1965).

just such variation, when it declared that the federal tax lien should be invalid as to "mortgagees". A mortgagee today is a person who has a lien that is given to him as security for the repayment of a loan, which lien becomes enforceable out of the property subject to the lien if and when the mortgagor defaults; and it is well established federal law that "State law creates legal interests and rights." *Morgan v. C. I. R.*³² There is nothing that requires a mortgagee in New Jersey to have the same interests and rights as a mortgagee in Arkansas. Therefore, to the extent that the interests and rights of a mortgagee in the one state vary from the interests and rights of a mortgagee in the other, the application of the "choateness rule" to competition between mortgage liens and federal tax liens may very well give rise to different results "depending upon variances in the terms and phraseology of different state and local * * * statutes and judicial rulings thereon"; and the counsel fee allowed in a New Jersey foreclosure action *can* be entitled to priority over a federal tax lien even though the counsel fee in Arkansas was not entitled to such priority. The result depends upon a clear understanding of the "choateness rule" and its proper application to each and every element of the lien of a mortgagee.

In Point II, B of appellant's brief, it is stated that "The United States conceded at the outset that the claims for the principal and interest under the mortgages had priority over the tax lien" (Pb7). Respondents are not willing to accept that concession in arguing this case, however, without a thorough investigation of the basis for the concession, to determine what there is about the principal and

³² 309 U. S. 78, 80, 84 L. Ed. 585, 588, 60 S. Ct. 424 (1940).

interest due on the mortgage that entitles it to priority over a federal tax lien when the United States is unwilling to concede priority to other items involved in the lien of a mortgage.

At page 8 of its brief, the United States says: "It follows that when the tax lien arose, respondent had no claim for attorney's fees, let alone a perfected lien for one. That claim remained a purely speculative contingency at least until default and the commencement of foreclosure proceedings."

There are at least three objections to this statement:

1. It fails to distinguish between a "claim" and an "enforceable claim."
2. It does not accord with the true nature of a mortgage lien.
3. It does not give adequate consideration to the reasoning applied by this court in its prior decisions relating to choateness.

1. The "claim" of the mortgagee.

No mortgagee has *ever* had a "claim" for *anything* that could be enforced out of the property described in the mortgage prior to the time that the mortgagor defaults in his primary obligation to repay the loan that the mortgage was given to secure. This statement is as true with respect to the principal and interest secured by the mortgage as it is true with respect to the counsel fee, or any other costs, involved in the foreclosure action which the mortgagee *must* bring if he wishes to enforce his "claim" after default by the mortgagor.

Therefore, if a mortgagee must have an "enforceable claim" at the time a notice of federal tax lien is filed, the protection given to mortgagees by Congress is almost completely illusory. Protection would be limited to those few cases in which default has occurred at a time sufficiently in advance of the filing of the notice of federal tax lien to permit the mortgagee to call the loan, order and receive the necessary searches, and commence an action—all in the face of convincing a court of equity that he has not been overbearing. Congress cannot be deemed to have enacted such useless legislation.

2. *The true nature of the mortgage lien.*

The United States fails to distinguish between the *creation* of a lien and the *enforcement* of a lien. In the case of a mortgage, the lien is created at the time the loan is made. The lien cannot be *enforced*, however, until the mortgagor defaults in his primary obligation to repay the loan in accordance with the terms of the bond or note. As soon as the mortgage is given, however, it is known that if the mortgagor does default, the only way the mortgagee can enforce the lien is to commence a foreclosure action and carry it through to a sheriff's sale. Thus, the lien of the mortgage, from the very outset, consists of the mortgage principal; the interest due thereon from the date the loan is made to the date on which the proceeds of the sale are received by the sheriff; all additional advancements made by the mortgagee pursuant to the terms of the mortgage, with interest thereon from the dates of the advancements to the date on which the proceeds of the sale are received by the sheriff; and all costs involved in the enforcement of the lien, including search fees, court costs, attorney's fees, advertising costs, and sheriff's fees and

commissions.⁵³ None of these items can be considered to be inchoate on the ground that enforcement of the lien has not reached a certain point in the proceeding by the time a notice of federal lien has been filed without destroying the lien, because the lien is the right to obtain repayment of the loan out of the property subject to the lien, and the mortgagee is powerless to commence an action until the mortgagor has defaulted.

Default of the mortgagor, then, is the *sine qua non* of enforcement of the mortgage lien. It has no bearing whatever either upon creation of the lien or upon choateness of the lien.

All of the items listed above exist as a basic and integral part of the mortgage lien, as to which, in the absence of some defect in the lien,⁵⁴ Congress has accorded priority; and the determination of choateness must be made with a test other than default of the mortgagor.

3. *The reasoning applied by this court in its prior decisions relating to choateness.*

At the time Congress acted to protect the mortgagee in 1913, there was nothing in the legislative history or in the

⁵³ The costs of enforcement would be nil if any of our fifty states recognized the common law mortgage. Prior to the founding of this country, however, the English Court of Chancery had abolished such mortgages as being too harsh.

The costs of enforcement would be lower in any of our states that recognize strict foreclosure or powers of sale in the mortgages. But our courts of equity or our legislatures, or both, have ruled out these procedures in most states, again on the ground that they are too harsh.

⁵⁴ Including inchoateness.

act itself to indicate that the rights of the mortgagee were dependent upon a finding that the mortgagee's rights amounted to a "choate lien". As we have seen, the concept of choateness of competing liens was first introduced into non-insolvency tax lien cases in 1950; and it was not until 1963, in *Piozeer*, that this court declared unequivocally that the "choateness rule" applies to mortgagees.

The definition of a choate lien was set forth in *New Britain* as follows:

"The liens may also be perfected in the sense that there is nothing more to be done to have a choate lien—when the identity of the lienor, the property subject to the lien, and the amount of the lien are established."⁵⁵

The definition includes three items: identity of the lienor, the property subject to the lien, and the amount of the lien. The United States, however, seeks to add a fourth requirement "that there is nothing more to be done". Its arguments ignore the rest of the phrase "to have a choate lien".

As we have seen, in the case of a mortgage there is nothing that *can* be done until the mortgagor-taxpayer defaults, and so we can dismiss default of the mortgagors as a requirement.

The United States contends, however, that it is necessary for judgment to be entered in the foreclosure action in order for the mortgagee "to have a choate lien". But judgment is merely one intermediate step in the judicial process whereby the equity of redemption is foreclosed. The judg-

⁵⁵ 347 U. S. at 84, 98 L. Ed. at 525.

ment, at least in New Jersey, merely fixes, as of a given date, the amount of principal and interest due on the mortgage, and the amount of the counsel fee computed according to R.R. 4:55-7(c), and then orders a sale of the mortgaged premises to raise the amount stated to be due to the plaintiff, with interest and costs, including the counsel fee. It is as necessary for the court to determine the amount of principal due as it is for it to determine the amount of the counsel fee. And thereafter it is necessary for the clerk of the court to compute the taxed costs.

But even then, the mortgagee has not realized anything from his rights under the mortgage. He must obtain an execution, which commands the sheriff to sell the mortgaged property at public sale. The sheriff is required to advertise the sale of the property for an extended period, and to conduct the sale. The mortgagee must make a substantial deposit⁵⁶ on account of the sheriff's costs; and, if a sale is held, the sheriff is entitled to commissions of 4% on the first thousand dollars of the purchase price and 2½% on the excess, and the sheriff's fees and commissions are entitled to payment over all other items.⁵⁷ The sheriff cannot deliver the deed for ten days, during which period any person in interest can move to have the sale set aside if he has an equitable ground for objecting to the sale.⁵⁸ In the absence of any such objections, the equity of redemption is thus foreclosed only when there has been an

⁵⁶ (Usually \$300 for the respondent first mortgagee in this case).

⁵⁷ N.J.S. 22A:4-8.

⁵⁸ New Jersey no longer requires confirmation of judicial sales. Confirmation was required in New Jersey until 1948, and is still required in many states. Until confirmed, the mortgagor retains the right to redeem.

actual sale of the mortgaged premises conducted by the sheriff of the county in which the lands are located. Then, and only then, is the mortgagee able to realize the benefit of the rights given to him under the mortgage; and in the meantime he has had to bear the entire burden of the expenses of the action. Throughout this entire period, the mortgagee's rights are limited by the extent of his lien.

The United States fails to recognize this function of the lien. At page 8 of its brief, it cites R.R. 4:82-5 in footnote 7, and states that "a mortgagee who commences and then abandons a foreclosure action loses his claim to attorney's fees even though junior encumbrancers proceed with the action."

If the mortgagee abandons the foreclosure action, he not only loses his claim for attorney's fees, but also his claims for principal, interest, and costs. The reason is obvious. If the mortgagor makes payment to the foreclosing mortgagee, the mortgagee is no longer required to enforce his lien.

The mortgagee, then, can *never* be in the position of "having nothing more to be done" until a sheriff's sale has been completed and the time for objection has expired. If the matter has proceeded that far, however, the mortgagee's rights have been completely satisfied or extinguished, and no lien is involved. There is no intermediate step in the foreclosure proceeding that can be said to mark the point at which "there is nothing more to be done", or at which the lien has been "perfected" in the sense implied by the United States at page 8 of its brief. The conclusion must be that the key to the problem of priorities is found in the words "choate lien", and that the definition of that term does *not* include the concept of whether "there is nothing more to be done".

The decisions of this court make it clear that the "choateness rule" involves only three items. In the case of a mortgage of specific property, it really involves only one because, barring an intrinsic defect, the identity of the lienor and the property subject to the lien are set forth in the mortgage. *The entire case, then, is reduced to a determination of what this court believes Congress intended should be necessary to establish the amount of the lien of a mortgage that will have priority over a federal tax lien recorded after the mortgage has been given.*

The amount of principal to be enforced through the mortgage can never be predicted prior to actual default. So long as the mortgagor fulfills his primary obligations on the bond or note, the principal amount will be reduced by whatever payments of principal are made, whether made according to an amortization schedule, or according to a prepayment privilege granted by the mortgagee. Thus, unless the mortgagor-taxpayer has defaulted prior to the time notice of a federal tax lien has been filed, it is impossible to fix the amount of the lien for principal, except in terms of a maximum amount that will be entitled to priority.⁵⁹

In terms of principal, however, the United States has refused to recognize that the maximum amount of mortgage principal entitled to priority over a federal tax lien is determined only when notice of the federal tax lien is filed. The answer of the United States filed in this action is identical with those filed in all such cases in the State of New Jersey known to respondents. That answer "disputes the

⁵⁹ In *Pioneer*, the mortgagors had defaulted prior to the time the notices of federal tax liens had been filed, and so it was possible to say that the principal of the mortgage was definite in amount. (374 U. S. at 92; 10 L. Ed 2d at 776).

priority * * * of any advances whatsoever made after the assessment dates of the lien of the United States''. (Tr. 4). Certainly when Congress declared federal tax liens invalid as to mortgagees until notice is filed, it recognized that the mortgagee needed the protection of notice whenever it should advance money, and it must have intended to include all items of principal that had been advanced by the mortgagee pursuant to the terms of the mortgage prior to the filing of the notice, whether the advance was made at the inception of the loan or at some future time prior to the filing of the notice of federal lien. Such later advancements are every bit as choate as the original advance made at the outset of the loan.

If the amount of principal to be obtained out of the property cannot be definitely fixed in amount prior to default by the mortgagor, the amount of interest is even more indefinite. In the case of interest, we cannot take the concurrence of an assumed default and filing of the notice of federal tax lien and then determine the amount of interest, for the interest will continue to accrue until the purchaser at the sheriff's sale has paid the full purchase price. No one can predict when such payment will be made until the very time at which delivery is made to the sheriff, and so we cannot even predict what the maximum amount of interest will be.⁶⁰ As we have seen, if the proceeding has

⁶⁰ Even though in *Pioneer* the mortgagors had defaulted prior to the time the notices of federal tax liens had been filed, the amount of interest could not be definitely established until the date of payment became known. Thus, the statement in *Pioneer* that the interest of the mortgage was definite in amount would have been incorrect if the phrase required an absolute dollar and cents figure. (374 U. S. at 92, 10 L. Ed. 2d at 776).

reached the point of payment of the purchase price after a sheriff's sale, we are no longer talking about a mortgage, a lien, or competition with a federal tax lien.

In *New Britain*, this court said that Congress intended that the priority of a competing lien "must depend upon the time it attached to the property in question and became choate". Therefore, when the United States concedes that the principal and interest secured by a mortgage have priority over the tax lien, it is conceding that these items meet the "choateness rule" established by this court, despite the fact that there is no time after the inception of the mortgage at which the exact amount of the lien that will be paid out of the property can be determined. The original principal amount and the rate of interest are known, from which computations can be made, but even the maximum amount of the lien cannot be determined until the proceeds of sale are received by the sheriff. Despite these elements of uncertainty, the government is correct in conceding, in effect, that the principal and interest secured by a mortgage are "choate liens", for otherwise §6323 (a) would be utterly meaningless.

There is absolutely nothing to distinguish the counsel fee allowed in New Jersey under R.R. 4:55-7 (c) from the interest secured by the mortgage. The interest is stated as a fixed percentage of the unpaid principal balance. Before the mortgagee can receive that sum out of the property, however, the mortgagor must default, a foreclosure action must be commenced, a judgment must be entered that fixes the amount due to the plaintiff and that directs a sale of the mortgaged premises, and the sale must be held and the purchase price received. These are the identical steps that must be taken with respect to the counsel fee. In each case,

the dollar amount will vary only in accordance with the number of payments made by the mortgagor prior to default, and the length of time between default and the entry of judgment (plus additional interest thereon to the date of actual payment to the sheriff).⁶¹

Despite the contrary contention of the United States, the counsel fee in this case is a far cry from the counsel fee in *Pioneer*. No one can dispute that a "reasonable attorney's fee" is not "fixed in amount". There is no standard by which to measure the dollar value of such a fee, and the allowance is made at the discretion of the court "for services rendered". With this court's declaration that a mortgagee is subject to the "choateness rule", the result of *Pioneer* could not be different. But the basis for the holding must still be, not that the attorney had to render services, but that there was no standard by which to measure, at the time the notice of federal lien was filed, the dollar amount of the lien of the counsel fee. In the present case, however, the lien of the counsel fee, which is not subject to being disallowed or varied in amount at the discretion of the court, could be computed to the penny at any time, merely by determining the number of payments made by the mortgagors and picking a date to which interest is to be computed.

⁶¹ Thus, for example, the mortgage in the present case was for \$30,000, with interest at 6% per annum on the unpaid balances from the date of the loan, December 13, 1960. If no payments were made by the mortgagors, the amount of a judgment for principal and interest computed to December 13, 1961, would be \$31,800 (\$30,000 principal and \$1,800 interest), and the judgment for counsel fee would be \$443 (3% of \$5,000, or \$150; 1½% of \$5,000, or \$75; and 1% of \$21,800, or \$218). The only assumptions that had to be made were a date on which the judgment would be entered and the number of payments made by the mortgagors.

The United States complains, however, that this counsel fee in New Jersey is a "‘formalistic device’ to which the collection of federal revenues may not be subjected," borrowing the descriptive words from *Buffalo Savings Bank*. (Pb5). For more than sixty years, however, New Jersey has had a rule similar to R.R. 4:55-7 (c). In the earlier years, however, the percentages were much lower, in keeping with the economics of the times.⁶² It is difficult to understand how a rule such as this, that was in existence prior to the act of Congress, and more than 50 years before this court declared that a mortgagee is subject to the "choateness rule", can be termed a "‘formalistic device’".

The United States also complains that the State of New Jersey can vary the percentages in the Rule. Such a change, however, would be no different than a change in the rate of interest in the mortgage. If the interest rate is changed

⁶² Prior to 1910, the rates were 1% on the first \$1,000; ½% on the next \$1,000; ¼% on the next \$3,000; and 1/5% on the excess over \$5,000.

The rule was amended effective February 1, 1910, and again effective January 1, 1917. These rules were identical as to percentages, but the italicized words in the text which follows were omitted in the 1917 amendment. *Rules of the Court of Chancery*, 147. "The percentage, *if any*, to be allowed in uncontested foreclosure cases, pursuant to the chancery act, is hereby prescribed by the Chancellor as follows, viz: on all sums decreed to be paid in such causes amounting to \$5,000 or less, at the rate of one per cent; upon the excess over \$5,000 and up to \$10,000 at the rate of one-half of one per cent; upon the excess over \$10,000 and up to \$25,000, at the rate of one-quarter of one per cent; and upon the excess over \$25,000 at the rate of one-fifth of one per cent: *provided that in cases where the complainant prevails after bona fide litigation a certificate to that effect may be made in the discretion of the Chancellor or Vice-Chancellor, in which case the complainant shall be entitled to double the above-mentioned percentages.*"

after a subsequent lien has attached, the increase may not be effective without the consent of the junior lienholder, but the mortgagee can recover interest at the original rate in any event. The principle involved is no different than that which is involved if the mortgagee makes an additional advance of principal. The mortgagee cannot increase the burden of a junior lienholder without his consent; but if there are no junior lienholders at the time the increase is made, subsequent junior lienholders are subject to whatever rights the prior lienholder had at the times they made their loans.

The United States claims that the distinction between the "reasonable fee" in *Pioneer* and the "precise method for determining the fee" in the present case "is without substance because * * * at the time the tax lien here arose there was no conceivable way of determining what sums or that any sum might some day be 'adjudged to be paid the plaintiff'". (Pb9). Only by conceding that principal and interest have priority over the tax lien, and then ignoring these items completely, however, is it able to make such a claim. The mortgagee has no rights whatever under the mortgage unless and until the mortgagor has defaulted, a foreclosure action has been commenced, and a court of equity has adjudged what sums are to be paid to the plaintiff. It has no more right to either principal or interest until those sums have been "adjudged to be paid the plaintiff in such [foreclosure] action", (Pb9), than it has to the counsel fee allowed under R.R. 4:55-7 (c).

In making this argument, the United States has failed to give adequate consideration to the reasoning applied by this court in its prior decisions relating to choateness. In the cases that did not involve a mortgagee, pledgee, pur-

chaser, or judgment creditor, Congress had not given priority to the lienholder. Therefore, the only way the lienholder could obtain the protection afforded when Congress required notice to be filed before the lienholder would be affected by a federal tax lien was for him to achieve the status of a judgment creditor.

The mortgagee, however, was given protection in his character as *mortgagee*, and there is no need for him to obtain the status of a *judgment creditor* unless his mortgage, or one or more of his rights, is intrinsically defective or is not fixed in amount, so that as to such right his lien is inchoate.

Finally, the United States complains about the amount of the counsel fee (\$425.52) in relation to the amount of the other items of taxed costs, and urges this as a ground for declaring the counsel fee as an "inchoate lien". It might better have objected to the payment of the sheriff's commissions, which were based upon the actual sale price of \$41,000. Under New Jersey statutes, the commissions were \$1,040, being 4% of the first \$1,000 and 2½% of the excess. This amount was computed in the same manner as the interest and the counsel fee, and was subject to every enforcement step required to be taken from the time of default to the actual receipt of the payment by the sheriff.

POINT II

The scope of the protection which Congress has given to mortgagees in 26 U. S. C. §6323 (a) embraces the counsel fee allowed under R.R. 4:55-7 (c) in New Jersey and all other elements of the mortgage lien which, on the date a notice of federal tax lien is filed, can be computed as to amount without making any assumptions other than a date to which interest is to be computed and that if the mortgagor had defaulted, his default was in payment of the item in question, it being immaterial whether or not the mortgagor has actually defaulted.

Since the advent of the "choateness rule" into the non-insolvency federal tax lien cases, mortgagees have been unable to enjoy any of the protection Congress intended to provide in 1913. The reason is that the United States, instead of examining the principles underlying the "choateness rule" when seeking to determine whether a competing lien is choate or inchoate, has chosen to attack specific items *per se*, without examining the characteristics of the particular items, and without regard to the variations in these items that exist because these items are created by state law.

There is no reason for mortgagees to continue to be denied the protection Congress thought it was giving them 53 years ago. If this court, in answering the question presented on this appeal, will define the "choateness rule" in relation to a mortgagee in such a clear-cut manner that there will be a definite standard by which all elements of a mortgage, and hence all rights of a mortgagee, can be judged, it will be possible to achieve this result.

In formulating the definition, it is important to make clear first that a mortgage lien includes all rights of the mortgagee—principal, interest, advancements made pursuant to the terms of the mortgage, and all costs and fees involved in the foreclosure proceedings, because the federal tax lien is not rendered invalid as to mortgagees, as Congress has declared it to be, to the extent that any right of the mortgagee is denied priority.

After the mortgage lien has been defined as embracing every right of the mortgagee, the definition of “choateness” suggested below can be applied to each right independently to determine whether or not it is entitled to priority. Respondents suggest the following definition:

If the amount of the item in question can be determined at the moment the notice of federal tax lien is filed, without making any assumptions other than (1) a date to which interest is to be computed, and (2) that if the mortgagor had defaulted, his default was in payment of the item in question, that item constitutes a “choate lien” and is entitled to priority over the federal tax lien, it being immaterial whether or not the mortgagor has actually defaulted.

Let us test the suggested definition.

Principal. All that is needed is a factual determination of the amount or amounts loaned to the mortgagor and the total payments on account of principal received by the mortgagee. The lien is choate.

Interest. All that is needed is a factual determination of the amount of unpaid principal and interest, plus the assumption of a date to which interest is to be computed. The lien is choate.

Counsel fee. In New Jersey, and in any other state having a similar statute or rule, in which the counsel fee is stated in fixed percentages and the allowance is mandatory rather than discretionary, all that is needed is a factual determination of the amounts of unpaid principal and interest, plus the assumption of a date to which interest is to be computed. The lien is choate.

In Arkansas, and in any state in which the counsel fee is stated in terms of reasonableness, or is allowed in the discretion of the court, the amount cannot be determined, and the lien is inchoate.

Other Costs of the Foreclosure Action. These items are usually provided by statute or court rule. Once it is known that a foreclosure action is to be commenced, they can be computed if all the facts are obtainable. Therefore, all that is needed is a factual determination of the rights of others to which the property is subject and the costs can then be computed. The lien of such costs is choate.

Advancements for Fire Insurance. All that is needed is the assumption that the mortgagor had defaulted in payment of the fire insurance premium, in which case the amount to be advanced can be computed.⁶³ The lien is choate.

Advancements for Necessary Repairs. All that is needed is the assumption that the mortgagor had defaulted in mak-

⁶³ Despite the fact that fire insurance premiums normally are not too large, and, if they are not paid the security for all liens, including the federal tax lien, is put in jeopardy, respondents' attorneys have been unable to obtain any assurance that the United States would not contest the priority of a fire insurance advance if the amount involved should be substantial.

ing necessary repairs, in which case the cost of the repairs can be determined. The lien is choate.

Advancements for Municipal Taxes.

a) Prior to the filing of the notice of the federal tax lien.

In its answer in the present case, and in all such cases known to respondents, the United States has ignored the Congressional act requiring notice in order to affect mortgagees, and has contested the validity of any advancements whatever after the assessment dates of the federal liens (Tr. 4). There is no basis for such a dispute, because the sums advanced have been made a part of the mortgage lien, and the identity of person, property, and amount are all known at the time the notice is filed. The lien is choate.

b) After the filing of the note of the federal tax lien.

Mortgages are given subject to a provision of state law that gives priority over all other state-created liens, including mortgages, to local tax, water, and sewer liens. Thus, even without the intervention of a federal tax lien, the value of the security held by the mortgagee is reduced to the extent of the unpaid local taxes and water and sewer rents. If the mortgagee has not seen fit to advance these delinquent items and make them a part of his mortgage, as provided in the mortgage, prior to the time a notice of federal tax lien is filed, there is no reason why he should receive the property free and clear of them if a federal tax lien has arisen, unless these items themselves are choate liens entitled to priority over the federal tax lien. In giving protection to the mortgagee, Congress did not intend to give the mortgagee more rights than he would have had if there had been no federal tax lien.

However, if, as in *New Britain*, there are some municipal liens that are entitled to priority over the federal tax lien, even in the hands of the municipality, there is no reason why a mortgagee whose lien also is entitled to priority over the federal tax lien should be denied the right to advance those taxes and retain priority, not only for its original mortgage, but also for the amount of such taxes added thereto, irrespective of when the mortgagee makes the advancement.

The principle is no different from that recognized by the United States in this case with respect to the first and second mortgages. As set forth in its brief (RA2a) it concedes that where there are two or more liens entitled to priority over the federal tax lien, the proper manner of setting up the rights of the parties is to establish a priority adjustment fund to be distributed according to state law, equal to the total of the sums due to each prior lienholder. Once the fund is set up, the United States concedes that it has no interest in the distribution of the fund. Therefore, if the second mortgagee wishes to advance the amount due to the first mortgagee, he would be able to claim the total funds due on both the first and second mortgages. So it is with a mortgagee who advances municipal taxes that have priority over the federal tax lien because they were assessed and became choate prior to the assessment of the federal taxes. Both the mortgage and the municipal tax liens have priority over the federal tax lien, and it is of no concern to the United States whether the municipality or the mortgagee is entitled to obtain payment out of the property. Under no circumstances, however, could the mortgagee advance taxes such as those in *Buffalo Savings Bank*, and obtain priority.

Thus, in the case of municipal liens that had not been advanced prior to the filing of the notice of the federal tax lien, the mortgagee could advance them and have a choate lien only if they had been assessed and had become choate prior to the time the assessment of the federal taxes was made. Priority would depend upon whether or not the municipality had a choate or an inchoate lien at the time of assessment of the federal taxes rather than at the time of filing of the notice of the federal tax lien. The mortgagee can protect himself by determining in advance whether or not the municipal taxes being advanced are choate or inchoate. If they are inchoate, he can proceed to immediate foreclosure in order to minimize the amount of taxes that will arise during the enforcement procedure.

Increase in rates of interest and percentages used in computing counsel fees and sheriff's fees. These items are essentially the same as advancements of principal. If the increase in rates was made before notice of a federal tax lien has been filed, the increased amounts would be choate liens; but if the increase in rates was made after the notice has been filed, the increased amounts would be inchoate liens.

* * *

The definition should go one step further and make clear that the "choateness rule" depends upon the existence of a federal *tax* lien. We have printed a portion of our trial court brief which refers to an answer filed in an action that involved a junior mortgage lien held by the United States of America acting through the Farmers Home Administration, in which the answer filed by the United States was identical to that filed in the tax lien cases (RA1a). On a motion for summary judgment, plaintiff prevailed, the court holding first that it believed the lien of the New Jersey

counsel fee to be choate, and second that it believed that the choateness rule was applicable only in tax lien cases. The United States took an appeal, and the parties contemplated bringing both appeals to this court at the same time. Prior to filing its brief, however, the plaintiff was advised that the solicitor general had ordered the appeal to be dropped.

In *Security Trust*, when this court first applied the "choateness rule" to a tax lien case, it said of the choateness rule that had theretofore been applied only in insolvency cases:

"If the purpose of the federal tax lien statute to insure prompt and certain collection of taxes due from tax delinquents is to be fulfilled, a similar rule must prevail here."⁶⁴

No such reason exists for imposing the "choateness rule" in a case in which the United States is the holder of a junior mortgage. In *New Britain*, this court recognized the "cardinal rule" that "a prior lien gives a prior claim, which is entitled to prior satisfaction, out of the subject it binds, unless the lien be intrinsically defective, or be displaced by some act of the party holding it, which shall postpone him in a Court of law or equity to a subsequent claimant."⁶⁵ It should be made clear that this is the only rule to be applied in non-tax lien cases, unless Congress has specifically provided for some other rule.

⁶⁴ 340 U. S. at 51, 95 L. Ed at 57.

⁶⁵ 347 U. S. at 85 and 86, 98 L. Ed. at 526.

CONCLUSION

The mortgagees in this case seek a ruling on the counsel fee in New Jersey foreclosure actions that is based upon a *principle* that can be applied to every right held by a mortgagee, stated in such clear terms that reasonable men cannot differ as to the results. They earnestly implore this court to relieve them, and all mortgagees, of the burden that has been thrust upon them because of the lack of an adequate definition of the "choateness rule" as it applies, not to municipal tax liens, landlords, or mechanics lien claimants, to whom Congress did not give protection from unrecorded federal liens, but to mortgagees, to whom Congress did give protection.

The definition suggested by the mortgagees in this case would put an end to the controversy between the United States and mortgagees. Its adoption would again restore to the mortgagees the protection which Congress intended to give them in 1913.

Respectfully submitted,

DONALD B. JONES,
Attorney for Respondents.

FRANK W. HOAK,
*Of Counsel and
on the Brief.*

April 5, 1966.

APPENDIX

Excerpt from Page 5 of Brief and Appendix for Plaintiff-Appellant

SUPERIOR COURT OF NEW JERSEY
APPELLATE DIVISION—DOCKET No. A-723-63

PRELIMINARY STATEMENT

The question presented by this appeal is narrow in scope, and involves the sum of \$425.52. The matter is of great practical significance, however, because the question is raised in several hundred cases per year—every time a mortgage is foreclosed on property affected by a federal tax lien.¹

* * *

¹ During the preparation of this brief, plaintiff has been served with an answer to a foreclosure complaint in which the United States, joined as the holder of a mortgage, granted by the Farmers Home Administration and subsequent in time to both the plaintiff's mortgage and to a judgment against the mortgagors, has disputed the allowance of counsel fees and advancements. Thus, the United States has expanded its contentions to include any lien held by the United States.

**Excerpt from Page 5 of Brief for United States of
America, Defendant-Respondent**

* * * It is however, recognized that under state law, the first mortgagee's claim for an attorney's fee is superior to the second mortgage. The resolution of this problem of circular priorities as established by the foregoing decisions is to provide for a priority adjustment fund in the amount of the principal and interest, plus costs, of the two prior mortgages under the federal order of priority. This amount is to be first set aside out of the proceeds of sale, but any excess over the priority adjustment fund must be first applied to satisfaction in full of the federal tax lien.* Once the priority adjustment fund is established, the Government has no interest in its distribution.

(* The question concerning the excess over the priority adjustment fund has never been decided in this case because it affects only the respondent second mortgagee, who has never been denied full recovery, and who would be denied full recovery only if this court should hold the lien of the counsel fee to be inchoate.)

SUPREME COURT OF THE UNITED STATES

No. 645.—OCTOBER TERM, 1965.

United States, Petitioner,	}	On Writ of Certiorari to the Supreme Court of New Jersey.
v.		
The Equitable Life Assur-		
ance Society of the United States.		

[June 6, 1966.]

MR. JUSTICE CLARK delivered the opinion of the Court.

This writ involves the recurring problem of priority contests between a state lien and a federal tax lien under §§ 6321 and 6322 of the Internal Revenue Code of 1954, 26 U. S. C. §§ 6321, 6322 (1964 ed.). Since 1950—*United States v. Security Trust and Savings Bank*, 340 U. S. 47—we have passed upon more than a dozen cases involving some facet of the problem. In the present case the law of New Jersey provides for the allowance in a foreclosure action of an attorney's fee fixed by statute as a certain percentage of the amount adjudged to be paid the mortgagee and taxed as costs in the action. The question presented is whether a federal tax lien is entitled to priority over the mortgagee's claim for such an attorney's fee, where notice of the tax lien is recorded prior to default by the mortgagor. The state trial court held that the federal tax lien was superior, New Jersey's highest court reversed, 45 N. J. 206, 212 A. 2d 25, and we granted certiorari, 382 U. S. 972. Only three Terms ago, Mr. JUSTICE WHITE writing for the Court, disposed of an almost identical question, i. e., whether "reasonable attorneys fees" provided for in a mortgage note "in the event of default . . . and of the placing of this note in the hands of an attorney for collection, or this note is collected through any court proceedings" created a lien superior

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to that of a federal tax lien recorded after suit on the note was filed but prior to the actual fixing of the amount of the attorney's fees. *United States v. Pioneer American Insurance Co.*, 374 U. S. 84 (1963). We there held the federal lien superior. We hold similarly here, and reverse.

I.

Albert Bagin and his wife executed to Equitable Life a first mortgage on certain real property in New Jersey. This mortgage, which secured an indebtedness of \$30,000, was recorded on December 19, 1960. The Bagins executed two other mortgages covering the property—a second mortgage which was also recorded on December 19, 1960, and a third, recorded on May 18, 1961. On March 21, 1962, the United States filed a tax lien for \$7,748.91 against Mr. Bagin. This lien, which was for unpaid withholding taxes, arose under 26 U. S. C. §§ 6321, 6322, and was recorded in accordance with 26 U. S. C. § 6323 (1964 ed.).¹ Shortly less than a year later, the Bagins

¹ These provisions state:

26 U. S. C. § 6321. LIEN FOR TAXES.

"If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, additional amount, addition to tax, or assessable penalty, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person."

26 U. S. C. § 6322. PERIOD OF LIEN.

"Unless another date is specifically fixed by law, the lien imposed by section 6321 shall arise at the time the assessment is made and shall continue until the liability for the amount so assessed is satisfied or becomes unenforceable by reason of lapse of time."

26 U. S. C. § 6323. VALIDITY AGAINST MORTGAGEES, PLEDGEES, PURCHASERS, AND JUDGMENT CREDITORS.

"(a) Invalidity of lien without notice.

"Except as otherwise provided in subsections (c) and (d), the lien imposed by section 6321 shall not be valid as against any mortgagee,

defaulted on the first mortgage and Equitable Life brought this foreclosure action. Equitable claimed the principal and interest due under the mortgage, as well as an attorney's fee as authorized by New Jersey statute.² The second mortgagee admitted the superiority of the Equitable Life's priority and demanded that the second mortgage be reported upon. Both the Bagins and the

pledgee, purchaser, or judgment creditor until notice thereof has been filed by the Secretary or his delegate—

“(1) Under State or Territorial laws.

“In the office designated by the law of the State or Territory in which the property subject to the lien is situated, whenever the State or Territory has by law designated an office within the State or Territory for the filing of such notice; or

“(2) With clerk of district court.

“In the office of the clerk of the United States district court for the judicial district in which the property subject to the lien is situated, whenever the State or Territory has not by law designated an office within the State or Territory for the filing of such notice; . . .

“(b) Form of notice.

“If the notice filed pursuant to subsection (a) (1) is in such form as would be valid if filed with the clerk of the United States district court pursuant to subsection (a) (2), such notice shall be valid notwithstanding any law of the State or Territory regarding the form or content of a notice of lien.”

² Rules Governing the New Jersey Courts (1965 ed.):

“4:55-7. Counsel Fees

“No fee for legal services shall be allowed in the taxed costs or otherwise, except:

“(c) In an action for the foreclosure of a mortgage. The allowance shall be calculated as follows: on all sums adjudged to be paid the plaintiff in such an action, amounting to \$5,000 or less, at the rate of 3%, provided, however, that in any action a minimum fee of \$75 shall be allowed; upon the excess over \$5,000 and up to \$10,000 at the rate of 1½%; and upon the excess over \$10,000 at the rate of 1%.”

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third mortgagees suffered default and their interests are not before us. The United States conceded the priority of the claims of the first two mortgages exclusive, however, of the attorney's fee, which it contended was inferior to the federal lien. The trial court rendered summary judgment fixing the sums due the respective parties and, viewing the priority question controlled by *United States v. Pioneer American Insurance Co.*, *supra*, subordinated the claim for attorney's fee to the federal tax lien. Without awaiting a sale of the property, respondent appealed to the Superior Court, Appellate Division, which certified the appeal to the Supreme Court of New Jersey. The Supreme Court ordered the property sold, and, after the sale, held that the statutory attorney's fee was superior to the federal lien.

II.

In *United States v. New Britain*, 347 U. S. 81 (1954), a leading case in this field, we held that where a debtor is insolvent the "Congress has protected the federal revenues by imposing an absolute priority" of the federal lien by virtue of § 3466 of the Revised Statutes (1875), now 31 U. S. C. § 191 (1964 ed.), and that where the debtor is solvent the "United States is free to pursue the whole of the debtor's property wherever situated" under 26 U. S. C. §§ 6321, 6322. *Id.*, at 85. The record here is silent on the solvency of the debtors, but as the priority issue below centered on §§ 6321-6323 we may safely assume they are solvent. As against a recorded federal tax lien, the relative priority of a state lien is determined by the rule "first in time is first in right," which in turn hinges upon whether, on the date the federal lien was recorded, the state lien was "specific and perfected." A state lien is specific and perfected when "there is nothing more to be done . . . —when the identity of the lienor, the property subject to the lien

and the amount of the lien are established." "Thus the priority of each statutory lien . . . must depend on the time it attached to the property and became choate." *United States v. New Britain, supra*. These determinations are of course federal questions. *United States v. Waddell Co.*, 323 U. S. 353, 356-357 (1945).

Pioneer American, supra, dealt with these identical problems and we therefore turn to its teachings. There, "the claim for the attorney's fee . . . became enforceable under Arkansas law as a contract of indemnity at the time of default . . . before the filing of the first federal tax liens." The suit in which the attorney's fee was earned was filed prior to the recording of the federal liens. "Nevertheless, because this fee had not been incurred and paid and could not be finally fixed in amount until . . . after all the federal liens had been filed," we held that the fees were "inchoate at least until that date and that the federal tax liens are entitled to priority." 374 U. S., at 87. As we said there, the attorney's fee was "undetermined and indefinite" at the time the federal lien was recorded; nor had the fee been "reduced to a liquidated amount." Moreover, there was no "showing in this record that the mortgagee had become obligated to pay and had paid any sum of money for services performed prior to the filing of the federal tax lien." Thus, the mortgagee's claim was not only "uncertain in amount" but "yet to be incurred and paid." *Id.*, at 90-91.

Equitable's statutory lien is even more clearly inchoate. At the time the federal lien was recorded Equitable's mortgage was not even in default—no reference whatever had been made to attorneys, no suit had been filed, nor had any sums been "adjudged to be paid." New Jersey's Rule 4:55-7 (c), *supra*, n. 2, which fixes the lien had not even been invoked much less applied to establish the amount of the lien. The claim was wholly contingent

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at the time the federal lien matured. Cast against the setting of *Pioneer American*, the inchoate character of the state-created lien here stands out even more starkly.

New Jersey's Supreme Court relied on the preciseness—the fixed percentages—of rule 4:55-7 (c), and applied the principle of *Security Mortgage Co. v. Powers*, 278 U. S. 149 (1928). It found *Pioneer American* inapposite. We cannot agree. *Security* did not involve a federal tax lien but raised "federal questions peculiar to the law of bankruptcy." 278 U. S., at 154. Our opinion in *Pioneer American* specifically pointed out that *Security* had no application to federal tax lien cases because the issue there was the status of an attorney's fee clause in a *bankruptcy* proceeding "where the rigorous federal lien choatness test was not necessarily applicable." 374 U. S., at 90, n. 8. We likewise find that *Security* has no bearing on the issue presently before us. As we noted earlier, at the time the federal lien matured here no sum of money due on the mortgage had been "adjudged." Adjudication alone triggers the mathematical machinery of Rule 4:55-7 (c) whereby liability for the attorney's fee is fixed. No liability having been incurred there could of course be no lien in existence at the time the federal lien matured. In short, the fixed fee of the statute had not been brought into play.

III.

Equitable Life's remaining contentions are also untenable. It argues that, since the United States concedes the priority of the mortgages here, the attorney's fee is likewise superior, for it must stand on no less equal footing as principal and interest under a mortgage—neither of which is ascertainable until foreclosure. This identical contention was raised and implicitly rejected in *Pioneer American*. There is nothing in the legislative

history of § 6323 indicating that in protecting mortgagees from secret, government tax liens, Congress intended to include all ancillary interests which a State may afford its mortgagees. See H. R. Rep. No. 1018, 62d Cong., 2d Sess. (1912). See also H. R. Rep. No. 1337, 83d Cong., 2d Sess. (1954); S. Rep. No. 1622, 83d Cong., 2d Sess. (1954).

Nor does the fact that New Jersey's statutory scheme taxes the attorney's fee as costs in the foreclosure proceeding affect the standing of a competing federal lien. To repeat, the relative priority of a United States lien for unpaid taxes is a federal question. *United States v. Acri*, 348 U. S. 211, 213 (1955). The label given the attorney's fee by the State does not bind this Court. As we said in *United States v. Buffalo Savings Bank*, 371 U. S. 228, 229 (1963), "the state may not avoid the priority rules of the federal tax lien by the formalistic device of characterizing subsequently accruing local liens as expenses of sale." Likewise in *Pioneer American*, the State was not permitted to upgrade its lien by the formalistic device of "indemnity." Even where authorized by state statute³ the distinction between costs and allowances for attorneys' fees is well recognized. In *Sioux County v. National Surety Co.*, 276 U. S. 238 (1928), the Court specifically noted this distinction in highly cogent terms: "That the statute directs the allowance [for attorney's fees] . . . to be added to the judgment as costs are added does not make it costs in the ordinary sense of the traditional, arbitrary and small fees of court officers,

³ Besides New Jersey, only three States provide explicitly for an allowance, as costs, for attorney's fees in foreclosure actions. 44 Iowa Code Ann. § 625.22; 7 Rev. Codes of Mont. § 93-8613; 46 Okla. Stat. Ann. § 56. Several others provide for the enforcement of contractually created claims for attorneys' fees in such actions, as in *Pioneer American*. See, e. g., VIII Conn. Gen. Stat. § 49-7; 4 Vt. Stat. Ann. § 4527.

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attorneys' docket fees and the like" At 243-244.⁴ Moreover, the mortgagee by foreclosing does not produce a fund from which the United States benefits, without expenditure on its part. A foreclosure is more akin to a liquidation of assets than to the creation, enhancement or protection of a common fund from which equity permits reimbursement of costs of litigation.⁵ Finally, it would be contrary to the federal policy of uniformity in the federal tax laws to permit the priority of federal tax liens to "be determined by the diverse rules of the various States." *United States v. Speers*, 382 U. S. 266, 270 (1965). See also *United States v. Gilbert Associates*, 345 U. S. 361, 364 (1953). While we believe that the established practice of awarding costs in the ordinary sense fairly renders those items an incident of the rights of those protected under § 6323, we see no warrant either in the intent of § 6323 or the practices prevailing among the States at the time of its enactment to treat attorneys' fees as a right entitled to priority over a federal tax lien.

⁴ Indeed, the Supreme Court of New Jersey has itself recognized this same distinction. In *United States Pipe and Foundry Co. v. United Steelworkers of America*, 37 N. J. 343, 355-356, 181 A. 2d 353, 359 (1962), that court stated that costs generally "comprise principally certain statutory allowances, amounts paid the clerk in fees, and various other specified disbursements of counsel including sheriff's fees, witness fees, depositions expenses and printing costs Counsel fees, although if allowable are included in the taxed costs, are an entirely different matter." (Emphasis added.)

⁵ In the latter case, courts proceeding under statutory or inherent equitable powers have traditionally awarded attorneys' fees. *Trustees v. Greenough*, 105 U. S. 527 (1881); *Sprague v. Ticonic Bank*, 307 U. S. 161 (1939). See McCormick, Damages § 62. In *Pioneer American*, we stated: "The attorney's services . . . were rendered for the benefit of the mortgagee to protect his interest in the property, and the United States, holding an adverse interest, received no such benefit from them that its interest is to be charged therefor." 374 U. S., at 92, n. 13.

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We hold that the federal tax lien is entitled to priority over the claim for the attorney's fee under Rule 4:55-7 (c). We intimate no view as to the disposition the state court may wish to make of the fund set aside for the principal, interest, and costs, exclusive of attorney's fee. That is a matter of state law. *United States v. New Britain, supra*, at 88.

Reversed and remanded.

MR. JUSTICE DOUGLAS dissents.